Market Commentary

PORTLAND INVESTMENT COUNSEL®

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News Highlights

Energy Sector

Whitecap Resources – increased its Viking, Saskatchewan, light oil exposure, by acquiring the privately held Beaumont Energy. It also raised $110 million in equity capital to finance the acquisition and provided increased 2015 guidance. Beaumont shareholders will receive 0.40 of a Whitecap common share for each Beaumont share and will have the option to take a portion of the consideration in cash up to maximum amount of $103.4 million. Whitecap will also be assuming the net debt of Beaumont, estimated at $70.5 million as at February 28, 2015. Based on an agreed upon Whitecap share price of $14.05 the total consideration including bank debt is $587.5 million. The company expects its 2015 average production to be 10% higher. Whitecap estimates the acquisition will be 6% cash flow per share accretive, on pro-forma leverage neutral basis. While acquisition metrics, both in term of production ($115k/boed) and 2P reserves ($18/boe) look full, Whitecap is buying a well known asset, offsetting current properties, with good well economics and 10+ years drilling inventory. Moreover, the company has a good track record of improving well performance (with waterflooding likely to be playing a big part) and increasing operating efficiency.

Earlier the company reported a robust set of results for its fourth quarter. Its cash flow per share of $0.54 was slightly ahead of consensus. Q4 production reached 37,000 boed (74% liquids). Whitecap maintained its 2015 guidance for 36,000 boed production on $200 million of capex. Company drilled 169 wells in 2014, with a 100% success rate. February's production, at 39,000 boed, is running ahead of the outlook and 2014 exit production. Production per share was 8% higher in 2014. Whitecap has 66% of 2015 oil production hedged at CAD91/bbl. As previously flagged, the company's credit facility was increased by 20% to $1.2 billion.

Pacific Rubiales Energy, the largest private oil producer in Colombia, said it would suspend paying dividends and that lenders had agreed to relax their terms, helping the company shore up funds to weather the slump in oil prices. The company, which cut its capital spending plans in January, said it would save about $52 million per quarter by suspending its quarterly dividend of 16.5 cents per share from the current quarter. Pacific Rubiales also said it had fully draw on its credit facility to pay off short-term bank debt for 2015 and 2016, pushing out the next payment to late 2016, and that it plans to hold the remaining funds of more than $500 million as a buffer against "a possible worsening oil price environment". The company said on Wednesday that lenders had agreed to relax terms to allow the company's debt to be 4.5 times its adjusted earnings before interest, taxes, depreciation and amortization (EBITDA) from the current 3.5 times adjusted EBITDA level. After rising for three quarters, the company's adjusted EBITDA fell 36% year-over-year to $419.3 million in the fourth-quarter ended December.

Financial Sector

ING - The Macquarie Group are interested in securing the remainder of ING's unbranded mortgage portfolio, worth A$1B , the Business Spectator reports. The Spectator reports Macquarie has previously bought three tranches of loans from ING in the last 18 months for A$4.6B and is seen as likely to buy the remainder of ING's unbranded portfolio by the end of the year.

Lloyds Banking Group plc notes the announcement by TSB Banking Group plc ('TSB') in relation to the agreed terms of the recommended cash offer for TSB Banking Group plc by Banco de Sabadell, S.A. ('Sabadell') pursuant to which Sabadell will acquire the entire issued and to be issued share capital of TSB (the 'Offer'). The Group has agreed to sell a 9.99% interest in TSB to Sabadell, and the Group has entered into an irrevocable undertaking to accept the Offer in respect of its entire remaining 40.01% shareholding in TSB. Under the terms of the Offer, TSB Banking Group plc shareholders will receive 340 pence per share in cash for each TSB share, which values the entire issued share capital of TSB at approximately £1.7 billion. António Horta-Osório, Group Chief Executive of Lloyds Banking Group plc, said: "I am delighted to confirm we have agreed terms for the sale of our remaining stake in TSB to Sabadell. This is a significant and positive step for the Group and will enable us to meet our commitments to the European Commission, well ahead of its mandated deadline." The Group currently owns approximately 50% of the issued share capital of TSB, which is held by Lloyds Bank plc ('Lloyds'), a wholly owned subsidiary of Lloyds Banking Group plc.

Canadian Dividend Payers

Northland Power and RWE Innogy announced that the €1.2 billion Nordsee One project has reached financial close, with all of the equity contributed to the project and all debt required for the project now fully committed by the project lenders. Northland owns 85% of the 332MW offshore wind farm to be located 40 kilometers off the coast of Germany, and RWE retains the remaining 15% interest. Approximately 70% of the project's required costs will be provided from an €840 million non-recourse secured construction and term loan and related loan facilities from ten international commercial lenders. Reflecting the strength of Nordsee One, the financing was oversubscribed. The lending group includes ABN AMRO, Bank of Montreal, Commerzbank, Export Development Canada, Helaba, KfW IPEX, National Bank of Canada, Natixis, Rabobank and The Bank of Tokyo-Mitsubishi. Nordsee One is entitled to a feed-in tariff subsidy under the German Renewable Energy Act. A substantial portion of the project returns are earned during the feed-in-tariff period, while the remainder of the planned returns are expected from the robust and mature German wholesale electricity market.

Global Dividend Payers

BHP Billiton said a proposed $13 billion spinoff of South32 would give the world's biggest miner a strong chance to ride out tough conditions in commodity markets and was a more attractive option than an asset sale. BHP released documents last Tuesday setting out the conditions for the split of its core iron ore, petroleum, copper and coal businesses from its non-core assets which will form South32, ahead of a planned listing in May. BHP has put far less debt than expected into South32, trying to ensure the company can weather the tough markets and still pay a dividend. BHP CEO, Mackenzie said the large diversified model that worked so well during the boom years was not fit for the current down cycle, in which sharpening the focus on productivity was a must.

South32, the new mid-sized miner, aims to focus on cutting costs and completing projects in its aluminium, manganese, silver and coal businesses before weighing up any new investments, despite a strong balance sheet and a market full of assets for sale. South32 will emerge from BHP with $674 million in net debt. Many in the industry think South 32 could be a takeover target for rivals or private funds such as X2, run by former Xstrata boss Mick Davis. Named after the line of latitude linking its two main centres, Australia and South Africa, South32 made up about 12% of BHP Billiton's total revenues in the year to June 2014. Mackenzie said it made sense to have two separate companies with different strategies, one focusing on huge assets with hundred-year lives, and the other with shorter-lived assets, processing plants and challenges in South Africa.

Procter & Gamble is reportedly exploring a sale or initial public offering of some of its beauty brands in a single deal. The maker of Pantene shampoo and Olay skin care is working on the plan with its advisers, but has not finalized details, including which products will be sold. P&G in August said it plans to sell about 90 to 100 brands with declining sales, focusing instead on 70 to 80 "core" brands, which account for most of its profit and revenue. The company's beauty products include the Aussie and Herbal Essences line of hair and body wash products, Covergirl makeup products and Head & Shoulders shampoo among others. P&G is working on turning around Pantene and Olay, its two largest beauty brands, and is likely to sell some fragrances, make-up and hair salon products. P&G, which also makes Gillette razors and Tide detergent, in November agreed to sell its Duracell battery business to Warren Buffett's Berkshire Hathaway. The company is also working with Goldman Sachs to explore the sale of its Wella hair care business, which could be worth around $7 billion, Reuters reported in November.

Rheinmetall plans a return to profitability this year for its defence unit, which was hit in 2014 by the withdrawal of an export licence for a training centre in Russia and provisions for potential warranty claims from a naval gun project. The German company said it targeted an operating profit margin of 3% for the defence unit this year, and 8% at its automotive division, which propelled group sales 6% higher last year and cushioned a fall in profits. Rheinmetall, which together with Krauss-Maffei Wegmann makes the Puma infantry fighting vehicles used by the German army, said group sales should rise to between €4.8 and €5 billion this year from €4.69 billion last year. But the dividend for 2014 will be cut to €0.30 euros per share from €0.40 euros. Rheinmetall reported last month that earnings before interest and tax (EBIT) fell to €160 million in 2014, or €102 million including special items from €213 million a year earlier. It said on Thursday its EBIT margin should rise to 5% this year from 3.4% last year, before special items.

Economic Conditions

US – US housing starts unexpectedly dropped in February, to a 0.9 million units annualized level, from January's 1.08 million, falling well short of the expectations for a 1.05 million reading. While most of the blame has been placed on weather, some other factors might also be at play; the National Association of Home Builders (NAHB) housing market index also surprised on the downside, reaching a 53.0 points reading in March, short of February's 55.0 points level and the 56.0 points consensus estimate, indicating that the US home builders are less upbeat about the industry prospects in the near term. Building permits for February, at 1.09 million units annualized, were slightly ahead of the expectations and an improvement over January's 1.05 million units annualized read.

US Federal Reserve on Wednesday opened the door further for an interest rate hike as early as June, ending its pledge to be "patient" in normalising monetary policy. But the US central bank signaled a more cautious outlook for US economic growth and slashed its projected interest rate path, in a sign that it remains concerned about the health of the recovery. In its statement following a two-day meeting, the Fed's policy-setting committee repeated its view that job market conditions had improved and gave its strongest signal to date that it was nearing its first rate hike since 2006. The statement put a June rate increase on the table, though it also allowed the Fed enough flexibility to move later in the year, stressing that any decision would depend on incoming data

Canada – Inflation in Canada continues to clock-in just above Bank of Canada's target range. The headline consumer price index (CPI) reading for February was flat, at 1.0% year on year, as expected, as significant gasoline price increases were partly offset by more stable prices for clothing, food and a retreat in the price of automobiles. The core CPI reading, which excludes eight most volatile price series, such as food and energy, retreated one notch to 2.1%, from 2.2% in January, in line with the consensus expectations.

January turned out to be worse than expected for the Canadian consumer, as retail sales retreated by 1.7% in the month, with some of the weakness caused by the drop in gasoline prices, but also slow auto sales. Core retail sales, which exclude sales of autos, were also weaker than expected, down 1.8%, dragged lower by sales of foods and drugs, offset by better sales in the clothing and electronics categories. The weak sales were chiefly caused by poor readings in Alberta and Sasketchewan, both likely affected in the low oil price environment.

Ireland the country that during the Great Recession needed to be bailed and needed to borrow money from the “Troika”, consisting of the IMF, ECB and the European Commission. Ireland only actually exited the bailout a little over a year ago. Of course, they didn’t actually “repay” the money they borrowed in the “bailout”, they were just able to win back the confidence of the market enough to go back to borrowing on their own. Now, 7 years after the crisis thanks to the efforts of the central banks, a country who needed to be bailed out (and borrowed a lot of money during that bailout) because the markets wouldn’t lend them money, is not only back to borrowing money on their own, but the market is paying them to borrow money. Ireland just sold €500M of public debt at negative yields with demand for 4 times that amount.

Italy - Reuters reports that Italy is planning to raise its official forecast for 2015 GDP growth to 0.7-0.8% from 0.6%.

UK - the recent Budget delivered by UK Chancellor of the Exchequer indicated expectations are for GDP to be 2.5% this year, up from 2.4% with 2016 also up from 2.2% to 2.3%. The UK is the fastest growing large country in Europe and although its deficit is high it is now expected that the national debt as a proportion of GDP will fall from 80.4% in the year to April 2016 to 71.6% by 2020. (Source:Financial Times)

Financial Conditions

US Federal Reserve policymakers remain determined to signal that although Quantitative Easing has stopped, the stimulus remains via keeping rates at present low until mid 2015. The US 2 year/10 year treasury spread is now 1.34% and the UK’s 2 year/10 year treasury spread is 1.12% - 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 US 30 year mortgage market rate has increased to 3.78% (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 US housing inventory is at 5.1 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 13.43 (compares to a post-recession low of 10.7 achieved in early June) 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 6 Mutual Funds:

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

Private/Alternative Products

Portland also currently offers 4 private/alternative products:

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

Net Asset Value:

The Net Asset Values (NAV) of our investment funds are published on our Portland website at http://www.portlandic.com/prices/default.aspx

Sources: Thomson Reuters, Bloomberg, Credit Suisse, KBW, Lloyds

Source:Thomson Reuters, Bloomberg, Credit Suisse, KBW, Lloyds

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