

News Highlights

Owners. Operators. And Insightful Investors.

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PORTLAND
INVESTMENT COUNSEL

Our views on economic and other events and their expected impact on investments

October 5, 2015

Energy Sector

Canadian Oil Sands -Suncor Energy Inc. commenced an unsolicited offer to Canadian Oil Sands Limited (COS) shareholders to acquire all of the outstanding shares of COS for total consideration of near \$4.3 billion. Under the terms of the offer, each COS shareholder will receive consideration of 0.25 of a Suncor share per COS share, representing a 43% premium based on closing share prices on Friday. Including COS' estimated outstanding net debt of \$2.3 billion as at June 30, 2015, the total transaction value is near \$6.6 billion. According to Bloomberg, this would be Suncor's second-largest deal after its purchase of Petro-Canada. Suncor last month bought an additional 10% stake in the Fort Hills oil-sands mining project from Total SA for C\$310 million. Canadian Oil Sands has the biggest stake in Syncrude, at 37%. Suncor owns 12%. We believe the proposed deal, alongside some of the other recent transactions in the sector, is a strong indication that the market participants see considerable value in oil and gas exploration and production companies, likely flagging a bottom in the valuation of the independent energy companies, which have been severely affected by the current crude oil prices environment.

Royal Dutch Shell – will focus its future investments in Nigeria on natural gas for domestic consumption and export, the managing director of the oil major's joint venture in the country said. "Our strategy is to invest a lot more in gas, for domestic consumption and export. We want to grow our deep water and constrain our onshore oil production," Osagie Okunbor told reporters in Port Harcourt, the country's oil hub. Shell has been divesting onshore oil-producing assets for the last few years and completed another set near the end of March. The sales are part of an effort to move away from onshore oil projects in Nigeria, which are plagued by industrial scale theft, security problems and pipeline spills, which have become a growing legal liability. Okunbor added that Shell's flagship project would be the Gbaran-Ubie project, which will increase gas supplies for the Bonny liquefied natural gas (LNG) export terminal. A first phase began production in 2010. Bonny is Nigeria's only LNG export terminal.

Energy major Shell is in talks to join Russia's state-controlled Gazprom in tapping the Yuzhno-Kirinskoye gas field offshore Russia's Sakhalin island in the Pacific. Last month, the United States restricted exports, re-exports and transfers of technology and equipment to the Yuzhno-Kirinskoye field. Lazare said Shell was complying with the sanctions, but "(we) don't change (plans) every five minutes". "We are continuing at the same pace. The approach is the same," he said of Yuzhno-Kirinskoye, which, according to Gazprom's plans, is set to be put upstream in 2018 and needs drilling machinery not produced in Russia. On Tuesday, Gazprom's deputy CEO Alexander Medvedev said in a Reuters interview the gas field would feed the Sakhalin-2 liquefied natural gas plant expansion - a Gazprom/Shell joint venture - as well as a pipeline to China from Sakhalin.

US oil demand – is likely to be helped by the U.S. auto sales, which surged in September to their strongest in more than a decade, with

the Detroit Three clocking double-digit growth as cheap gasoline and ultra-low interest rates drove demand for sport utility vehicles and pickup trucks. Sales also got a boost from the calendar, with the entire Labor Day weekend falling in September for the first time since 2012. Total vehicle sales for the month shot up 15.8% from a year earlier to 1.44 million cars and light trucks, equal to a seasonally adjusted annual rate, or SAAR, of 18.17 million, according to research firm Autodata Corp. That topped estimates for a SAAR of 17.6 million and was the highest since the 20.6 million clocked in July 2005. At this pace, the U.S. auto industry is on track to challenge the record for full-year sales of 17.8 million vehicles set in 2000. "The U.S. is adding jobs, disposable income is rising, energy prices and interest rates remain low and business continues to invest, but the fact remains this has been a slow recovery," said Mustafa Mohatarem, GM's chief economist. "The economy still has room to grow and so do auto sales, particularly now that the millennials are entering the workforce and starting households," he added. Ford's total sales rose 23% to 221,599. Ford-brand SUV sales increased 27%, the best in 12 years, while trucks sales increased 23.2%. Fiat Chrysler's sales increased 14% percent to 193,019, boosted by the continued strength of its Jeep SUV brand. Jeep sales jumped 40%. "On the back of a strong sales industry we were able to achieve our best September sales in 15 years and our 66th-consecutive month of year-over-year sales growth," said Reid Bigland, head of the company's U.S. sales. Research firm LMC Automotive in late September raised its forecast for full-year U.S. car and light truck sales to 17.2 million vehicles from 17.1 million. While low gas prices seem likely to continue to help sales of SUVs and pickups such as the Chevrolet Silverado and Ford F-150, the days of near-zero interest rates look set to end as the Federal Reserve considers raising rates for the first time since 2006. Strong auto sales could help hasten that decision.

Energy Infrastructure – Canadian regulators approved the hydrotest results of Enbridge Inc's Line 9 crude oil pipeline, clearing the way for the delayed 300,000 barrel-per-day route to the east of the country to start operating. The newly reversed Line 9 will ship mainly light inland crude from Sarnia, Ontario, to Montreal, Quebec. It previously flowed in the opposite direction, taking imported crude to Ontario. The line, originally expected to start up in late 2014, was held up after the National Energy Board ordered hydrostatic tests at three locations along the line in June. The Line 9 approval is a rare bright spot for backers of Canadian pipeline projects, which include TransCanada Corp's Keystone XL and Enbridge's Northern Gateway. The approval was welcomed by the Canadian Association of Petroleum Producers and Suncor Energy, which owns a refinery in Quebec and is one of Line 9's biggest customers.



Financial Sector

Ares Capital Corporation announced plans to redeem \$200 million of 7.75% unsecured notes due 2040 on 10/28/15. The repayment will be funded with its low cost credit facilities. In addition, \$805 million of convertible debt yielding 5.57% is expected to be replaced with new 5-year unsecured debt that recently was priced at 3.875%. The combined annual savings is expected to \$0.11 per share.

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Ares Capital announced its Board of Directors has approved a stock repurchase program. Pursuant to the program, Ares Capital is authorized to repurchase up to \$100 million in the aggregate of its outstanding common stock in the open market at certain thresholds below its net asset value per share. Ares Capital expects that the program will be in effect until September 30, 2016, or until the approved dollar amount has been used to repurchase shares.

Barclays PLC is in preliminary discussions with potential buyers to exit from parts of its investment banking business in Brazil, Sky News reported citing people familiar with the matter. Barclays' executives have greenlighted a process to explore an exit from its Brazilian operations and deal talks are set to open, Sky News said. (Source Reuters). Barclays is exiting its non-core Bmarkets business in Europe as part of a wider strategy review it unveiled last year. The company said in a statement Bmarkets, designed to help distribute financial products in France, Italy, Germany and Switzerland, had been designated non-core in the review presented in May last year. "In line with its strategy, Barclays is now announcing its intention to exit its Bmarkets business," it said. (Source: Reuters).

Berkshire Hathaway – Warren Buffett has cut his stake in German reinsurer Munich Re after warning earlier this year that prospects for the reinsurance industry had turned gloomier. Buffett's companies Berkshire Hathaway Inc. and National Indemnity Company cut their combined holding to 9.7% from around 12% previously. It was unclear whether Buffett plans further reductions in his stake, which he built from less than 3% to more than 10% in 2010. In May, he told Berkshire Hathaway shareholders that the reinsurance business was "unlikely to be as good as it was". "We are pleased that Warren Buffett has been a significant shareholder for many years," Munich Re Chief Financial Officer Joerg Schneider said, adding the reinsurer would ensure that its shareholders would continue to be spread over many countries and investor groups.

Citi announced a multi-year agreement to launch a private label consumer credit card program for Wawa. Wawa owns and operates more than 700 convenience stores (over 450 offering gasoline) in 5 Mid-Atlantic states and Florida. The companies expect to launch the card program on Sept 30 with Citi managing and servicing the portfolio of accounts. The agreement with Wawa is the 4th new card relationship (Volkswagen, Brooks Brothers, Costco) and 7th contract renewal (American Airlines, Tractor Supply Co., Brand Source, Goodyear, Office Depot, Expedia) Citi has announced since the beginning of 2014. Citi also has offerings with Best Buy Macy's, Sears and The Home Depot, among others.

Royal Bank of Scotland - CEO Ross McEwan says Royal Bank of Scotland could buy back its own shares to help the Government offload its 73% stake in the bank. The Government sold a 5.4% stake in RBS at a loss of £1bn in August and has targeted the sale of three-quarters of its stake in the next five years. "I would rather participate as the Government is selling down ... I think it's probably the best thing for all investors, where excess capital goes back through buy-backs," Ross

McEwan told the Bank of America Merrill Lynch Banking & Insurance Conference in London. "At some stage, we'd like to put a dividend policy in place" and "it's probably the best thing for all investors, where excess capital goes back through buyback. You've seen very good examples of that in the marketplace." RBS targeting dividend in 1Q, 2017. Also, Royal Bank of Scotland - Applied for a banking license for Williams & Glyn ahead of an IPO in 4Q16. Application to FCA, PRA has 16,000 pages, includes business strategy, risk and governance, financial reporting. "This banking license application shows our regulators that we're building a safe and sound bank with robust processes," Chief Administration Officer Simon McNamara says in statement

Total Loss Absorbing Capacity - Bloomberg reported that the Financial Stability Board (FSB) has taken some decisions regarding the final rules for the total loss absorbing capacity (TLAC) rules, ahead of its final announcement at the G20 meeting in November. Based on this article, the final TLAC rules will require G-SIFI (Global systemically important financial institution like JP Morgan, Barclays) banks to reach TLAC of 16% (as percentage of Risk Weighted Assets) by 2019 (excluding the G-SIFI buffer), rising to 18% by 2022. This is positive in our view as it is in the middle of the previously proposed range of 16-20%.

Activist Influenced Companies

Nothing to report this week.

Canadian Dividend Payers

Canfor Corp. announced that they have entered into an agreement to purchase El Dorado, Arkansas-based Anthony Forest Products ("AFP") for a purchase price of U\$93.5mm – in the 12-months ended August 2015, AFP generated EBITDA of U\$16mm – in its most recent fiscal year ended April 30, 2015, AFP's EBITDA came in at ~U\$19mm – it's estimated EBITDA and EPS accretion of 2.3% and 2.8% respectively in 2016 and 2.7% and 3.3% in 2017 estimated -- while Canfor currently trades at ~7.0x LTM EBITDA, the AFP purchase price of U\$93.5mm implies an EV/LTM EBITDA multiple of ~5.8x -- pro-forma the acquisition, Canfor's U.S. South capacity grows to 1,640 mmbf, up from 1,390 mmbf (27% of total lumber vs. 24% previously) – overall, we believe the acquisition is consistent with Crown's U.S. South expansion strategy and provides them with access to high quality fibre supply in Arkansas, Louisiana, and Georgia, where stumpage costs as a % of reference lumber prices have fallen in recent years – this is in stark contrast to the steady increase that stumpage costs in the BC interior have experienced since 2010. In our view industry themes remain little changed, as unsustainably low lumber prices are expected to continue to precipitate N.A. production curtailments and ultimately pull supply into line with demand -- for building products exposure, we continue believe Canfor represents an attractive investment in the Portland Global Dividend Fund.

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Global Dividend Payers

AT&T Inc, the No. 2 U.S. wireless carrier, said it expects to report more than 2 million net subscriber additions for the third quarter, with gains in every category including postpaid and prepaid. AT&T also expects to report positive U.S. net subscriber additions for the recently acquired satellite TV provider DirecTV, it said in a regulatory filing. AT&T, which reported 2.1 million net wireless additions in the second quarter, said in August that it expected revenue, earnings and free cash flow to grow through 2018 following its purchase of DirecTV and wireless expansion in Mexico. AT&T said it expects capital spending to increase from second-quarter levels. AT&T also said it would change the methodology DirecTV used to count its commercial subscribers to conform to its practices, which will reduce DirecTV's total subscriber count by 918,600 at the close of the deal in July. The company also reaffirmed its forecast for full-year adjusted profit and revenue growth.

AT&T may take a charge estimated at \$1.1 billion related to DirecTV's Venezuela assets in what is the latest U.S. company to confront the South American country's currency woes. The plunging value of Venezuela's currency cut nearly \$3 billion in profit at U.S. blue-chip companies during the second quarter and prompted Procter & Gamble Co to remove its operations in the South American country from its consolidated financial reports. In July, AT&T completed its \$48.5 billion merger with DirecTV to become the largest U.S. pay-TV company. AT&T has said previously that the primary value of the deal is in DirecTV's U.S. business. The value of DirecTV's \$1.1 billion in Venezuelan assets is currently based on an exchange rate of 12 Venezuelan bolivars per U.S. dollar. AT&T said it may value the assets at the so-called Simadi exchange rate of about 200 bolivars per U.S. dollar, according to the SEC filing. Revaluing those assets at the less preferential Simadi rate would erase nearly all of the value of those Venezuelan assets, AT&T said. Venezuela introduced the Simadi rate in February as part of a currency devaluation. With slumping crude oil prices and debt payments coming due this year, the Venezuelan government has fewer U.S. dollar reserves available to meet the private sector's demands. In the first quarter of 2015, DirecTV's Venezuela operations generated \$200 million in revenue and operating profit before depreciation and amortization of \$75 million. Had DirecTV used the Simadi rate for that quarter, those operations would have reported an operating loss, AT&T said in a filing.

GEA has lowered its 2015 revenue guidance slightly (EBITDA guidance unchanged). The company no longer expects organic revenue growth in 2015, but does expect growth including FX and M&A. We are expecting total growth in 2015 of 3% with organic growth of -4%. The revised 2015 revenue guidance ("growth including FX and M&A") implies an organic revenue decline of upto 5-6% in our view. GEA has maintained its 2015 EBITDA guidance of EUR590-640m excluding the impact from FX and M&A. Consensus is at EUR633m (including both). The company says that its lowered revenue guidance reflects a further global economic slowdown, particularly in emerging economies

including China. We don't believe this comes as a big surprise. Management express a cautious tone as macro uncertainty has led customers to adopt a "wait and see" approach to capex spending, notably in emerging markets.

Novartis – The U.S. Food and Drug Administration has accepted Novartis unit Sandoz's regulatory submission for approval of a biosimilar copy of Amgen's blockbuster Enbrel drug. Biosimilars aim to copy biologic products, which are made inside living cells, but they can never be exact duplicates, so biosimilar manufacturers need to conduct clinical trials to show their products work as intended. Enbrel, or etanercept as the drug is known generically, is a big prize since it was the world's fifth-biggest selling medicine in 2014 with sales of nearly \$9 billion. Amgen, which sells the drug in North America, booked Enbrel sales of \$4.7 billion last year. Pfizer sells Enbrel elsewhere. Merck and Samsung Bioepis last month won approval for biosimilar etanercept in South Korea and a copy is also on the way in Europe, where Samsung is working with Biogen, but Sandoz said it believed it was the first company to receive a U.S. FDA file acceptance. Sandoz is seeking approval for all indications included in the label for Enbrel, a so-called anti-TNF drug, which is used to treat a range of autoimmune diseases including rheumatoid arthritis and psoriasis, it said in a statement. Novartis last month launched the first biosimilar drug in the United States after a U.S. appeals court declined to stop the sale of the company's copycat version of Amgen's blockbuster cancer drug Neupogen. Insurers and government healthcare systems hope biosimilars will cost the public 40% to 50% less than the original drugs and experience in Europe suggests that steep discounts are being offered in some markets.



Economic Conditions

US – The US purchasing managers index (PMI) report issued by the Institute for Supply Management (ISM) for the month of August was barely in the 'expansionary' territory, at 50.20 index points, below the expected 50.60 value and almost an index point below July's 51.10 read. This is the lowest reading since May of 2013, with weakness broadly based across this composite index.

U.S. nonfarm payrolls rose only 142,000 in September, and August's gain was surprisingly lowered to 136,000 (from 173,000; July was also marked down by 20k to 223,000). This is well below average job growth in the first seven months of the year (214k). The softness was widespread, with manufacturing down for a second straight month and the service-providing sector slowing in the past two months after leading job creation earlier this year. Household survey employment plunged 236,000, more than erasing the prior month's gain. The jobless rate stayed at a 7½- year low of 5.1% only because of an even larger drop in the labour force (-350k after -41k in July, the third drop in four months). The participation rate plummeted to a new 38-year low of 62.4%. The lower job growth in the past two months, supports the Fed's recent actions to stall any rate increase. While consumer spending has come back strong, the weakness in manufacturing

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suggests the economy isn't firing on all cylinders, largely because the US dollar and sluggish global demand are undercutting net exports. This will raise questions about whether the economy can continue to grow at its recent strong pace. Unless rebounding job growth in the next two reports clears up this uncertainty, the Fed could in our view be on hold in December as well.

Canada – Canadian economy expanded by 0.3% in July, beating expectations for a 0.2% improvement and building on June's strong 0.4% advance. Growth was supported by a rebound in mining and oil and gas activity, but also by the transportation, finance and manufacturing sectors. Utilities, agriculture and professional services subtracted from growth in the quarter.



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 earliest September 2015. The US 2 year/10 year treasury spread is now 1.42 and the UK's 2 year/10 year treasury spread is 1.20% - 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 3.86% (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 5.0 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 20.14 (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 Investment Counsel Inc. currently offers 7 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
- Portland Value Fund

Private/Alternative Products

Portland also currently offers private/alternative products:

- Portland Focused Plus Fund LP
- Portland Private Income Fund
- Portland Global Energy Efficiency & Renewable Energy Fund LP
- Portland Advantage Plus Funds
- Portland Private Growth Fund

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, KBW, Credit-Suisse, Scotiabank, Barclays, BMO



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Source: Thomson Reuters, Bloomberg, KBW, BMO, Credit Suisse, Macquarie, Barclays, TD, NBFInancial

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