News Highlights

Owners. Operators. And Insightful Investors.

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Established in 2007

PORTLAND INVESTMENT COUNSEL®

Our views on economic and other events and their expected impact on investments. May 22, 2018

Owner Operated Companies

Linamar Corporation – We met with the management of Linamar last week, in advance of the company's announcement of its first quarter results. The investment thesis for Linamar remains intact, with strong growth trends seen in its addressable markets, driven by a significant shift towards outsourcing by the OEM (original equipment manufacturers) of powertrain and driveline components, as the OEMs are focusing their efforts on the integration of the newest available technologies, such as digitization, electrification and autonomous driving. Linamar has line of sight for $8.5 billion to $9.0 billion worth of revenue by 2022, from the current $6.5 billion (for 2017). The company has seen significant business wins in Europe and Asia, including two large orders for full electrical vehicle gearboxes for one million units by 2023, which is the equivalent of about 20% global market share. The increased adoption of nine and ten speed transmissions has led to record levels of content per vehicle (CPV) for the manufacturer.

Sales for Linamar's first quarter of 2018 were $1,893.9 million, up $237.9 million from $1,656.0 million in Q1 2017. Sales for the transportation segment increased by $127.3 million, or 9.3% in Q1 2018 compared with Q1 2017. The industrial segment product sales increased 38.6%, or $110.6 million, to $397.5 million in Q1 2018 from Q1 2017 chiefly due to the acquisition of Canadian agricultural equipment manufacturer - MacDon Industries Ltd. The company's operating earnings for Q1 2018 were $214.9 million. This compares with $192.2 million in Q1 2017, an increase of $22.7 million. "We are thrilled with another quarter of record sales growing in double digits and record levels of content per vehicle in every region," said Linamar chief executive officer Linda Hasenfratz. "We are particularly happy to see double-digit operating earnings growth as well despite lower markets in North American automotive and unfavourable exchange rate changes. The key to continuing our strong performance is an intense focus on new business wins which we are delivering on in spades in the most opportunistic sourcing environment in the automotive sector we have ever seen. Concurrently, excellent growth opportunities in robust markets for our Skyjack and MacDon businesses is painting an excellent picture of global prosperity for Linamar in the future."

Energy Sector

Crescent Point Energy Corp. revealed its intention to divest its working interests in oil and gas assets located in Bottineau County, North Dakota, U.S. The sale includes operated working interest in 143 wells (102 producing, four non-producing, four salt water disposals, 23 plugged and abandoned, 6 temporarily abandoned, 3 abandoned, one drilled) and 15,583.88 net leasehold acres (HBP) located in Williston Basin. The assets have a six-month average production of approximately 859 boed and 397,000 cubic feet per day. EnergyNet.com, Inc. has been retained by the company for the divestment of the assets. The bid is due on June 13, 2018. The sale is part of the well flagged divestment program, aiming to raise roughly $1 billion in proceeds for the 2018, which is likely to be used to reduce the company's debt load.

Whitecap Resources, Inc. – The Toronto Stock Exchange has accepted the notice of Whitecap's intention to commence a normal course issuer bid (NCIB). Whitecap previously purchased an aggregate of 2,502,322 common shares at a weighted average price per share of $8.76 under a normal course issuer bid that runs between May 18, 2017, and May 17, 2018. The NCIB allows Whitecap to purchase up to 20,864,806 common shares (representing 5% of its 417,296,134 outstanding common shares as of May 4, 2018) over a period of 12 months commencing on May 18, 2018. The total number of common shares Whitecap is permitted to purchase is subject to a daily purchase limit of 455,083 common shares, representing 25% of the average daily trading volume of 1,820,333 common shares on the TSX calculated for the six-month period ended April 30, 2018, however, Whitecap may make one block purchase per calendar week which exceeds the daily repurchase restrictions. Any common shares that are purchased under the NCIB will be cancelled upon their purchase by Whitecap. Whitecap believes that, at times, the prevailing share price does not reflect the underlying value of the common shares and the repurchase of its common shares for cancellation represents an attractive opportunity to enhance Whitecap's per-share metrics and thereby increase the underlying value of its common shares to its shareholders. Whitecap will use the NCIB as another tool to enhance total long-term shareholder returns and will be used in conjunction with management's disciplined free funds flow capital allocation strategy.

Financial Sector

Barclays PLC announced this morning that the Crown Court today has dismissed all charges brought by the Serious Fraud Office (SFO) regarding matters which arose in the context of Barclays 2008 capital raisings - specifically (i) conspiring with former officers to commit fraud by false representation relating to agreements with Qatar Holdings and (ii) provision of unlawful financial assistance relating to a $3 billion loan provided to State of Qatar. Whilst an incremental positive, we expect the SFO to apply to the High Court to reinstate the proceedings limiting the extent to which this is net positive. **Meanwhile last week Chief Executive Jes Staley** was fined just £642,430 by regulators for breaching rules by trying to identify a whistle-blower. The Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) said he failed to "act with due skill, care and diligence" in his response to an anonymous letter received in June 2016. The FCA and PRA began their probe into Mr. Staley's conduct a year ago. Barclays said it would cut his bonus by £500,000. Directors delayed deciding how much Mr. Staley's bonus would be docked until the investigation was complete and they knew the penalty imposed. Mr. Staley said: "I have consistently acknowledged that my personal involvement in this matter was inappropriate, and I have apologised for mistakes which I made. I accept the conclusions of the board, the FCA, and the PRA, following their respective investigations, and the sanctions which they have each applied." (Source: BBC)

Barclays will package up and sell on the £4 billion ($5.4 billion) worth of Irish home loans that it bought from U.K. rival Lloyds Bank PLC on Friday, in a sign of the resurgent appetite for securitized mortgages that played a big role in the 2007-2008 financial crisis. The deal marks the second large-scale mortgage securitization this year for the lender, after a group led by Barclays in April bought £5.3 billion worth of residential mortgages from the British 'bad bank' set up to manage the assets of two failed lenders. It shows the continuing trend of European banks selling assets to investors such as hedge funds and private equity firms, as they attempt to shrink their balance sheets to focus their businesses and comply with tougher capital regulations. Barclays has already lined up a group of investors to buy the former Lloyds loans, according to Cecile Hillary, head of Barclays' asset finance business which it opened last year. (Source: Reuters)

Fifth Third Bancorp announced the purchase of MB Financial Inc., a Chicago-based middle-market commercial bank (though with an emphasis on customers smaller than Fifth Third's traditional focus), for $4.7 billion (approximately 20% of its market cap), a 24% premium to Friday's close. The price equates to 2.8x tangible book (highest multiple in recent memory) and 16.4x 2019 EPS. The purchase adds scale to Fifth Third's operations in Chicago and affords it the ability to leverage its product and service capabilities to MB Financial's customer base while realizing cost savings (45%) and increasing its financial targets (18%+ ROTE). MB Financial has $20 billion in assets and increases Fifth Third's footings by 14% to $162 billion. It increases Fifth Third's Chicago market share from 3.6% (8th) to 6.5% (4th) and more than doubles its Chicago deposit contribution (11% to 24%). Tangible book dilution is expected to be 8% ($1 billion). Assuming a year-end close, Fifth Third management believes the purchase will be 2% EPS accretive in 2019 and 7% additive in 2020. It is now targeting an 18%+ ROTE and sub-56% efficiency ratio, with the fully phased-in transaction impact in 2020. In addition, its Capital Adequacy plans and new 3rd-party driven efficiency program are not expected to be impacted. Still, between the two efficiency programs at Fifth Third (NorthStar and consultants), another round of branch closures, MB Financial's mortgage restructuring, and now a large-scale merger integration, Fifth Thirds has a lot on its plate in our view.

HSBC Holdings PLC said last Monday it has performed the world's first trade finance transaction using a single blockchain platform, in a push to boost efficiency in the multi-trillion-dollar funding of international trade. HSBC and Dutch bank ING Groep N.V. completed the deal for Cargill Inc. last week when a shipment of soybeans was transported from Argentina to Malaysia via the global commodities trader's Geneva and Singapore subsidiaries, the British lender said in a statement. While there have been other trade finance deals that use blockchain in conjunction with other technologies, the Cargill transaction marked the first use of a single, shared digital application rather than multiple systems, HSBC said. The use of blockchain technology in the banking industry is expected to reduce the risk of fraud in letters of credit and other transactions as well as cut down on the number of steps used. (Source: Reuters)

JPMorgan Chase & Co. said last Monday it has applied to China's securities regulator to set up a securities business in which the U.S. bank would own a majority stake under recently relaxed ownership rules. The unit, in which JPMorgan would own 51%, would allow the firm's corporate and investment banking divisions to seek more Chinese clients on the mainland in an effort to expand and grow their businesses, JPMorgan said in a statement. The U.S. bank also said it is looking to double its research coverage of China-listed companies across all sectors, and that it has appointed banking veteran Mark Leung as chief executive of its China business. The application is a step toward JPMorgan's return to the securities business in China, having sold its 33% holding in a similar venture to its local partner in 2016. JPMorgan did not disclose who would own the remaining 49% of the new venture. However, it said it would raise its ownership to 100% if eventually permitted. **JPMorgan shareholders last Tuesday** voted to reelect all directors on the bank's board at its annual shareholder meeting in Plano, Texas, with each director receiving at least 88% of the vote. Shareholders also voted to approve bank Chief Executive Officer Jamie Dimon's compensation, with 93% voting yes. During a wide ranging question-and-answer session, Dimon told shareholders the bank would review investments in private prisons and an oil drilling project in the Amazon rainforest. (Source: Reuters)

Royal Bank of Scotland Group PLC - CEO is considering restarting dividends (which has been known since results were released) but on a scale that would make it one of Britain's most generous payers to shareholders and would be likely to accelerate the government's sale of its holding. (Source: The Times)

Activist Influenced Companies

Brookfield Business Partners L.P., together with institutional partners, has completed the previously announced acquisition of a controlling interest in Schoeller Allibert Group B.V., one of Europe's largest manufacturers of returnable plastic packaging systems. Brookfield Business Partners is a business services and industrials company focused on owning and operating high-quality businesses that benefit from barriers to entry and/or low production costs. Brookfield Business Partners is the flagship listed business services and industrials company of Brookfield Asset Management Inc.

Dividend Payers

Brookfield Property Partners L.P. is, reportedly, in talks to acquire a stake in a Manhattan office tower majority-owned by a company that was previously run by Jared Kushner, son-in-law of U.S. President Donald Trump. Brookfield, one of the world's largest real estate companies, would oversee the redevelopment of 666 Fifth Avenue, a 41-storey tower controlled by Kushner Companies. Brookfield would oversee a significant redevelopment of the building if a deal was reached.

Wal-Mart Stores, Inc. latest quarterly results show total revenue increased +4.4% with constant currency sales higher by 2.7% year/year. The gross margin was lower by 15 basis points (bps) and operating expenses were 11 bps higher as a percent of net sales. Operating income of $5,154 million declined 1.6% year/year. Operating income on a constant currency basis of $5,030 million declined 4.0% year/year. Adjusted EPS was $1.14, growth of 14% year/year. Adjusted EPS excludes an unrealized loss of $0.47 on the company's equity investment in JD.com, Inc. due to a change in accounting principles. The second item benefited EPS by $0.05 due to an adjustment in the provisional amount recorded in Q4 2018 related to Tax Reform.

Economic Conditions

Canada homes resales fall in April, lowest in over five years: Last week, Reuters highlighted a report from the Canadian Real Estate Association (CREA) showing resales of Canadian homes fell 2.9% in April, to the lowest level in more than five years. CREA said actual sales, not seasonally adjusted, fell 13.9%, while the group's Home Price Index was up 1.5% from April 2017. The once-hot housing market has cooled in recent months in response to rising interest rates and tighter mortgage rules, while most economists expect a soft landing, some say there is a risk of a U.S.-style crash. About 60% of local markets reported fewer sales, led by the Fraser Valley area of British Columbia, Calgary, Ottawa and Montreal. The number of newly listed homes fell 4.8% in April to hit a nine-year low for the month, 12% below the 10-year monthly moving average, CREA said. The national sales-to-new listings ratio firmed slightly to 53.7% from 52.6% in March. A ratio between 40% and 60% is considered a balanced market. There were 5.6 months of inventory, the highest level since September 2015, CREA said. Prices in the Greater Toronto Area were down 5.2% from April 2017, while a still-hot condo market helped drive Greater Vancouver prices 14.3% higher compared to a year earlier. The national average price for homes sold in April 2018 was just over CAD $495,000 ($383,453), down 11.3% from a year earlier, CREA said.

Canada's consumer price index (CPI) rose 0.1% (month/month) in April in seasonally adjusted terms causing the year/year inflation rate to decline one tick to 2.2%. This was below consensus expectations calling for a 2.3% annual rate. On a month/month basis, five categories were rising with alcohol/tobacco, clothing, and household operations experiencing the strongest increases while recreation, healthcare and transportation posted declines. CPI excluding food and energy was flat in seasonally adjusted terms and the year/year inflation rate declined one tick to 1.8%. On an annual basis, the CPI-trim stood at 2.1% (up one tick from 2.0%), CPI-Median at 2.1% (up one tick from 2.0%) and CPI-Common at 1.9% (unchanged).

U.S. - China trade war. While China has not agreed to meet the U.S.'s demand to reduce the bilateral trade deficit by $200 billion over two years, it has pledged to buy more U.S. products (notably farm and energy goods) and reduce tariffs on some other products (notably autos, to 15% from 25%), putting the risk of a trade war "on hold", according to Treasury Secretary Mnuchin.

U.S. retail sales rose 0.3% in April, while sales excluding autos were up a like-sized 0.3%. Although the results were more or less in line with expectations, the upward revisions to the prior two months gave this report a more positive glow. The gains were fairly broadly based, but a couple of categories, which reflect discretionary spending, stood out in a negative light: two consecutive declines (albeit very small) in sales of sporting goods/hobbies, while dining out also saw a drop. Core spending rose an as-expected 0.4%.

Italy's president is, today, in talks as the country awaits news about whether an unknown law professor without any political experience will be approved as the next prime minister. The country's two populist parties, the Five Star Movement (M5S) and the League, announced a joint agreement naming Giuseppe Conte, an M5S member, as the next leader. This comes after Matteo Salvini of the League, and Luigi Di Maio of the M5S, ruled themselves out. Conte requires the approval of the country's president, Sergio Mattarella, who met with Salvini and Di Maio on Monday evening and will hold further meetings today. The parties' agenda calls for sweeping fiscal changes, a more confrontational stance against Brussels, and a tougher approach against migrants, including the creation of detention centres across the country.

Financial Conditions

The U.S. 2 year/10 year treasury spread is now .49% and the U.K.'s 2 year/10 year treasury spread is .68% - 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 costs of capital.

Influenced by the withdrawal of quantitative easing, the U.S. 30 year mortgage market rate has increased to 4.61% (was 3.31% end of November 2012, the lowest rate since the Federal Reserve began tracking rates in 1971). Existing U.S. housing inventory is at 3.6 months supply of existing houses. So the combined effects of low mortgage rates, near record high affordability, economic recovery, job creation, and low prices are still supporting the housing market with housing inventory well off its peak of 9.4 months and we believe now at the low end of a more normal range of 4-7 months.

The VIX (volatility index) is 12.99 (compares to a post-recession low of 9.52 achieved in early November) and while, by its characteristics, the VIX will remain volatile, we believe a VIX level below 25 augurs well for quality equities.

And Finally

Congratulations Harry and Meghan ...... Diana would be delighted.

Mutual Funds

Portland Investment Counsel Inc. currently offers 8 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
- Portland 15 of 15 Fund

Private/Alternative Products

Portland also currently manages the following private/alternative products:

- Bay & Scollard Development Trust
- Portland Advantage Plus - Everest and McKinley Funds
- Portland Focused Plus Fund LP
- Portland Focused Plus Fund
- Portland Global Aristocrats Plus Fund
- Portland Global Energy Efficiency and Renewable Energy Fund LP
- Portland Global Sustainable Evergreen Fund
- Portland Global Sustainable Evergreen LP
- Portland Private Growth Fund
- Portland Private Income Fund
- Portland Special Opportunities Fund
- Portland Value Plus Fund

Individual Discretionary Managed Account Models - SMA

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

We want to share our insights with you and welcome your feedback. Our website has the latest, as well as archived videos, company profiles, and press articles. Please visit us at www.portlandic.com.

Glossary of Terms: 'boe' barrel of oil equivalent, a measurement of a unit of energy, 'boed' refers to barrel of oil equivalent per day, 'CET' core equity tier, 'EBITDA' earnings before interest, taxes, depreciation and amortization, 'EPS' earnings per share, 'FCF' free cash flow, 'ROE' return on equity, 'ROTE' return on common equity.

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