

News Highlights

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PORTLAND
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Established in 2007

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

June 11, 2018

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Owner Operated Companies

Berkshire Hathaway Inc. – Berkshire Hathaway Inc., Amazon.com, Inc. and JPMorgan Chase & Co. within the next two weeks will likely name a chief executive for their joint venture aimed at lowering the cost of health care. Buffett, who is Berkshire Hathaway's chairman, and JPMorgan Chief Executive Jamie Dimon said in the interview that they had selected a person for the healthcare venture's top job. Famed for his love of junk food, Buffett has described U.S. healthcare costs as a "tapeworm" on American businesses, hurting their ability to compete with rivals in other countries. Last month, he said the goal is to challenge the entire healthcare industry, not individual segments. "We've basically reached agreement," Buffett said. "We should have an announcement on that matter within maybe two weeks." While there is no guarantee the venture between Amazon.com, Berkshire and JPMorgan, which collectively employ more than 1 million people, will succeed in lowering costs, Buffett said it was well positioned to try. "The resistance will be unbelievable, and if we fail, at least we tried," Buffett said last month.

Brookfield Asset Management Inc. (BAM) – We had the opportunity to re-connect with a number of our asset management holdings during a conference in Toronto last week, including BAM, Brookfield Business Partners L.P. (BBU), Blackrock Inc. and IGM Financial Inc. BAM touted its unique positioning in managing assets in property, infrastructure and private equity globally through the use of its private funds. The company sees its private fund business as a key growth driver, with significant room to grow. BAM has an established private funds business which, to date, raised over \$100 billion of commitments from a select group of about 500 clients, including some of the world's most renowned wealth funds, pension plans, endowments and foundations. Included is a roughly \$32 billion commitment of its own capital, which has gone a long way towards providing confidence for deal partners, whether be it in larger sized infrastructure deals or individual real estate transactions. A key component of Brookfield's strategy is its value focused private equity business. BBU, who recently invested in Scholler Allibert, Group B.V. one of Europe's largest manufacturers of returnable plastic packaging systems. BBU seeks to take advantage of company's under stress; a prime example being one of its most recent and prominent deals, the acquisition of Westinghouse Electric Company LLC, out of bankruptcy proceedings. BBU often leverages the larger BAM platform for sourcing, due diligence and execution. In addition, something that may not be immediately apparent, BBU draws on its own and group's expertise as owner-operators of assets. For example, prior to the acquisition of Graftech International Holdings

Inc., a producer of graphite rods for steelmaking which had fallen on hard times, BBU had operated steelmaking assets and had followed Graftech for a long time before proposing a deal on favourable terms. Similarly, the OLG bundle acquisition was based on Multiplex' development expertise and the fact that Brookfield had been operating casinos in Las Vegas and Bermuda. BBU has currently about \$1.7 billion which could be deployed in accretive deals around the world.

Fortive Corp. – Johnson & Johnson (J&J) said Fortive Corp. had offered to buy its medical sterilization unit for about \$2.7 billion in cash. J&J has been reviewing its portfolio of businesses and had recently said it was nearing a sale of its diabetes device unit for \$2.1 billion. J&J's advanced sterilization products (ASP) business, part of its Ethicon Inc. unit, generated revenue of about \$775 million in 2017. The drug maker said it had 120 days to accept the offer and, if it does so, the deal would be expected to close no later than early 2019. For Fortive, which makes industrial products, the deal would provide an entry into the "strong growth" medical sterilization and disinfection market. The company said it planned to finance the acquisition through debt or equity and with available cash. It also expects the deal to add to adjusted earnings in the first full year after the transaction. The Goldman Sachs Group Inc. was the financial adviser to Fortive, while Sidley Austin LLP and Wilmer Cutler Pickering Hale and Dorr LLP served as legal advisers.

Energy Sector

Iran sanctions – European refiners are reportedly winding down oil purchases from Iran, closing the door on a fifth of the OPEC member's crude exports after the U.S. imposed sanctions on Tehran. The drop in crude purchases from the Islamic republic could complicate efforts by European governments to salvage the Iranian nuclear deal disavowed by U.S. President Donald Trump last month. Although European governments have not followed Washington by creating new sanctions, banks, insurers and shippers are gradually severing ties with Iran under pressure from the U.S. restrictions, making trade with Tehran complicated and risky. Trump on May 4 announced his decision to quit the landmark 2015 nuclear deal between Iran and world powers and reimposed sanctions on Tehran. The restrictions on Iran's oil sector take effect after a 180-day "wind-down period" ending on November 4. Ministers from Germany, France and Britain have urged U.S. officials to shield European companies from the sanctions, but refiners are not taking any chances. Refiners including France's Total S.A., Italy's Eni and Saras, Spain's Repsol and Cepsa as well as Greece's Hellenic Petroleum S.A. are reportedly preparing to halt purchases of Iranian oil once sanctions bite. These refiners account for most of Europe's

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purchases of Iranian crude, which represent around a fifth of the country's oil exports. Iran's crude sales to foreign buyers averaged around 2.5 million barrels per day in recent months, according to data collected by Reuters and EU statistics office Eurostat. The bulk of the exports go to Asia. Iranian crude can be substituted by Russian Ural grades, whose prices have risen following the U.S. announcement, as well as crude from Saudi Arabia. Asian buyers are also expected to reduce their purchases. India's Reliance Industries Ltd, owner of the world's biggest refining complex, reportedly plans to halt oil imports from Iran.

Financial Sector

Royal Bank of Scotland Group PLC (RBS) - Following last Monday's announcement, U.K. Government Investments has sold 925 million shares in RBS equivalent to 7.7% reducing the Government holding from 70.1% to 62.4%. Sold at 271 pence equivalent to 3.5% discount to yesterday's close with gross proceeds of £2.5 billion. 90 day lock-up. Budget expectations of approx. £3 billion per annum. from the Government over the next 5 years. The price was determined by way of an accelerated bookbuilding process. Bookrunners named below not to sell further shares in the company for a period of 90 calendar days following the completion of the Placing without the prior written consent of a majority (by participation) of the Bookrunners. Citigroup Inc., Goldman Sachs International, J.P. Morgan Securities PLC and Morgan Stanley International PLC have been appointed to act as joint bookrunners in connection with the Placing. Settlement and delivery of the Shares is expected to take place on June 7, 2018. Subsequently, RBS's - CEO says the bank hopes to buy back stock to reduce U.K. stake. In comments at Frankfurt conference, the CEO was confident the lender will pass this year's stress test.

Activist Influenced Companies

Pershing Square Holdings Ltd. (PSH) – announced that the company has been advised by Pershing Square Capital Management, L.P. that CEO Bill Ackman and PSH Board Member Nick Botta have purchased additional PSH public shares. Since May 29, 2018, Mr. Ackman has purchased a total of 10,804,142 public shares at an average price of \$14.79 per share. Mr. Ackman currently owns 6,645,150 management shares which are convertible into 7,091,986 public shares. If these management shares were converted to public shares, Mr. Ackman would own a total of 17,896,128 public shares, representing approximately 8.1% of the Company on a fully diluted basis assuming all management shares are converted into public shares.

Dividend Payers

Roche Holding AG - The U.S. Food & Drug Administration (FDA) approved Venclexta plus Rituxan for 2L+ CLL, with or without 17% deletion, based on the phase 3 MURANO study. Venclexta previously received accelerated approval for the treatment of patients with relapsed/refractory CLL with 17% deletion. Today's FDA approval converts Venclexta's accelerated approval to a full approval. Venclexta is jointly commercialized by AbbVie Inc. and Roche in the U.S. and commercialized by AbbVie outside of the U.S. This is the first-of-its kind chemotherapy-free targeted therapy for patients with 2L+ CLL.

South32 Limited has agreed to its first material acquisition since listing, a 50% interest in the Eagle Downs met coal project in Queensland for \$106 million upfront cash, a \$27 million deferred payment 3 years after closing and a production-based royalty capped at \$80 million. It's estimated the acquisition is at a Price/NPV multiple of 0.36x and a 17% Internal Rate of Return (IRR) – overall we view this as a very attractive use of surplus capital in a commodity the company knows well. It also adds a growth option to an otherwise ex-growth portfolio. South32's balance sheet is well positioned to fund the deal with \$1.9 billion of net cash at March 2018. Eagle Downs is a coking coal project in Queensland's Bowen Basin located near BHP's Peak Downs mine. It has had various owners over the last 10 years. Vale S.A. acquired a 50% interest in the project from Advanced Micro Controls Inc. in 2007 with the balance owned by Aquila Resources Inc., a publicly listed company subsequently acquired by Baosteel (now China BaoWu Steel Group Corporation) in 2014. South32 is acquiring its stake from BaoWu as an on-sale of Vale's stake. Vale and Aquila completed a feasibility study on the project in 2011 and subsequently spent approximately AUD \$200 million (USD \$150 million) on mine development before suspending activity in 2015. The construction of mine access is 40% complete via two 2km long drifts down to the coal seam, plus surface and water infrastructure. The asset is likely to be relatively small, contributing an estimated \$129 million attributable EBITDA, or approximately 6% of our current EBITDA forecasts once in full production from 2024.

Economic Conditions

U.S. trade deficit narrowed more than expected and for the second straight month in April, albeit from multi-year highs in February. The deficit fell by a billion dollars to \$46.2 billion, putting it just below the past-year mean. Exports rose 0.3%, adding to sizeable gains the prior two months, though they fell slightly in real terms. For the most part, exports of goods and services have trended higher in

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the past year (+9.9%) on the back of earlier weakness in the dollar and firmer global demand. Meantime, imports slipped for a second straight month (in real terms, too), though they are still up 8.0% year/year. Purchases of capital goods rose in the month and are up 10.3% in the past year, reflecting increasing business investment.

The U.K. Report on Jobs, a survey of recruitment consultants, for May indicates strong growth in demand for staff while the availability of suitable candidates continues to fall. Growth in permanent placements remains high but was the least marked in 2018, while the rate of growth in temporary billings was the highest since last December. Average starting salaries continues to increase. The rate of growth in permanent salaries is the highest in three years while growth in pay for temporary staff is close to last month's two-year record. The report's Vacancy Index, a measure of demand for staff, saw growth reach a six-month high, where demand remains higher in the private sector than the public sector.



Financial Conditions

The Reserve Bank of Australia (RBA) has left interest rates unchanged at the historic low of 1.5% for the 20th consecutive meeting. The current holding pattern is the longest stretch without a move, with the RBA last changing rates with a 25 bps cut in August 2016.

The U.S. 2 year/10 year treasury spread is now .43% and the U.K.'s 2 year/10 year treasury spread is .66% - 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 4.54% (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 4.0 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 12.32 (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.

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.

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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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