# News Highlights

*Owners. Operators. And Insightful Investors.*

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*Established in 2007*

PORTLAND INVESTMENT COUNSEL®


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## Owner Operated Companies

**Alphabet Inc.** reported second-quarter revenue and earnings which beat analysts' expectations. Alphabet, which generates about 85% of its revenue from sales of ad space and ad technology, reported total second-quarter revenue of $38.9 billion. That was up 19% over last year and compared with 17% growth in the first quarter. Analysts on average estimated 16.8% growth and $38.2 billion in revenue. Alphabet authorized up to $25 billion in new stock buybacks, aiming to make use of its $121 billion in cash. CEO Sundar Pichai said quarterly revenue from licensing cloud computing services and workplace software jumped to about $2 billion, from its last disclosure of $1 billion at the end of 2017. He said the cloud unit would triple its sales staff over the next few years. Net income for the second quarter rose to $9.95 billion, or $14.21 per share, compared with analysts' estimates of $8.02 billion, or $11.32 per share. Alphabet's quarterly costs at $29.76 billion were about flat with the same period a year ago. The operating margin was 24%, up from 18% in the first quarter.

**Facebook, Inc.** reported second quarter results which included above-expectations revenue. Its namesake app is producing growth even as users gravitate toward newer, more private features whose popularity has outstripped their usage among advertisers. Second-quarter revenue rose to $16.9 billion from $13.2 billion a year ago, beating analysts' average estimate of $16.5 billion. For the quarter, Facebook reported 2.7 billion monthly users and 2.1 billion daily users across Facebook, Messenger, Instagram and WhatsApp, both figures about the same as last quarter. Facebook announced it agreed to pay $5 billion to settle a U.S. Federal Trade Commission (FTC) data privacy probe, but then disclosed that the regulator was now investigating it for anti-competitive behaviour. The settlement suggested that Facebook had moved past a major regulatory challenge that has dogged it over the last year. Facebook, which had set aside $3 billion in the first quarter for the settlement, said it took a $2 billion charge in the second quarter to account for the remainder. The FTC payment in part cut second-quarter profit to $2.6 billion, compared with $5.1 billion a year earlier. Excluding the settlement and a $1.1 billion one-time tax expense, earnings would have been $1.99 per share, Facebook said. The expectations for its ad business and cost forecasts could hurt profit margins, particularly in the fourth quarter, Facebook said.

**Fortive Corporation** reported second quarter results, which included net earnings from continuing operations attributable to common stockholders of $158.1 million. For the same period, adjusted net earnings from continuing operations were $322.3 million. Diluted net earnings per share from continuing operations were $0.47. For the same period, adjusted diluted net earnings per share from continuing operations were $0.90. Revenues from continuing operations increased 16.4% year/year to $1.9 billion, with core revenue growth of 2.0%. James A. Lico, President and Chief Executive Officer, stated, "Today we reported second quarter results which reflected an 18% year-over-year increase in adjusted diluted earnings per share. We achieved the high end of our guidance despite slowing in our short-cycle businesses which became more pronounced as we progressed through the quarter. In the face of these emerging headwinds, our more resilient portfolio and the strength of the Fortive Business System helped to deliver another quarter of strong earnings growth and free cash flow." For the full year 2019, Fortive expects diluted net earnings per share from continuing operations to be in the range of $2.12 to $2.27. For the full year 2019, Fortive expects adjusted diluted net earnings per share from continuing operations to be in the range of $3.45 to $3.60. Mr. Lico added, "Our performance in the second quarter reflected the growing contribution from the acquisitions we have closed over the past few years, including Advanced Sterilization Products which made a solid start in its first quarter under Fortive ownership. These acquired businesses continue to perform well, improving our growth profile and reducing the cyclicality across our portfolio, while also enabling us to deliver sustained double-digit annual earnings growth."

## Energy Sector

**Crescent Point Energy Corporation** announced second quarter results which exceeded expectations on cash flow generations, primarily driven by lower operating costs and a better hedging position relative to last year's comparative period. Production reported was roughly in-line with the expectations, when accounting for the production generated by assets divested in the quarter. The company continues to pursue divestments of both non-core productive assets and infrastructure assets. Crescent Point reduced net debt by over $450 million year-to-date 2019, primarily driven by excess cash flow and disciplined capital spending. 'Our second quarter results continue to demonstrate our focus on disciplined capital allocation, realizing cost efficiencies and strengthening our balance sheet,' said Craig Bryksa, President and CEO of Crescent Point. 'We expect to generate significant excess cash flow in 2019, allowing for net debt reduction and accretive share repurchases. We continue to target additional asset dispositions as part of our focused asset strategy, providing increased efficiencies and financial flexibility.' Adjusted funds flow totalled $503.8 million or $0.92 per share diluted during the second quarter, based on a strong operating netback of $36.59 per boe. For the quarter, Crescent Point's capital expenditures on drilling and development, facilities and seismic totalled $166.2 million, including $146.5 million on drilling and development to drill 52 (39.8 net) wells. Net debt as at June 30, 2019 equated to approximately $3.6

billion or 1.9 times trailing adjusted funds flow. Cash and unutilized credit capacity as at June 30, 2019 was approximately $2.0 billion, with no material near-term senior note debt maturities.

## Financial Sector

**The Bank of America Corporation (BofA)** and UBS Group AG have reshuffled their investment banking teams in a bid to muscle in on fundraising and advisory work for private companies, as businesses put off going public and fees from initial public offerings come under pressure. Both banks have this month created new teams focused on capital raising and advice to privately owned businesses, according to memos seen by the Financial Times. The moves reflect how early introductions to such companies have become increasingly important as Wall Street banks look to generate revenues from advising on initial public offerings and mergers and acquisitions. BofA and UBS are hoping to join the small cadre of Wall Street giants — led by **Goldman Sachs, Morgan Stanley and JPMorgan Chase** — setting their sights on young companies that traditionally rely on venture capital firms for early backing. "The volume of capital being raised in the private markets is approaching amounts raised in the public markets," Thomas Sheehan and Jack MacDonald, co-heads of global investment banking at BofA wrote in a memo to its staff. "We must identify and cover these companies much earlier in their lifecycle." (Source:Financial Times)

**Fifth Third Bancorp** reported second quarter EPS of $0.57. Excluding $84 million of merger-related expenses and a $17 million negative valuation of Visa total return swap, EPS was $0.71. Consensus was $0.66. Relative to its guidance, net interest income was above (GAAP NIM higher), while loans, core Net Interest Margin, fee income (top end of the range) and expenses (better end of the range) all approximated expectations. Its tax rate was lower than expected and its loan loss provision was below consensus (though non-accrual loans up $71 million, or 16%, albeit from a low base). Linked quarter, period-end loans (-0.5%) and its commercial line utilization rate (to 37% from 38%) both declined. It booked $8 million in securities gains and $2 million in securities gains for non-qualifying hedges on Mortgage Servicing Rights. Operating revenues increased 21% year/year and rose 17% linked quarter to $1.9 billion, driven by a full-quarter of its purchase of MB Financial, Inc. (closed March 22). Tangible book expanded 7.5% to $20.03 (trading at 1.4x). It posted an adjusted ROTCE of 15.8%. Its CET 1 ratio declined 2 basis points (bps) to 9.58%. Shares outstanding decreased by 9.2 million shares. In the second quarter of 2019, its average diluted share count increased 11.5%, while period-end shares declined 1.1%. Its adjusted efficiency ratio was 58.5%. Its loan loss provision declined $11 million to $78 million. Its reserve/loan ratio was unchanged at 1.02%.

## Activist Influenced Companies

Nothing significant to report.

## Dividend Payers

**AT&T Inc.** beat Wall Street estimates for net post-paid wireless subscribers as it continues to bundle media content from Time Warner Inc. into new wireless plans. The second-largest U.S. wireless carrier by subscribers added a net 72,000 phone subscribers, bigger than analysts' estimates of 27,000 subscribers. AT&T closed its $85 billion acquisition of media company Time Warner in June last year, creating a new business segment called WarnerMedia to house assets including the Turner TV networks and premium channel HBO. The new WarnerMedia segment reported revenue of $8.4 billion during the quarter, while analysts were expecting $8.30 billion. Total operating revenue in the second quarter rose to $45 billion from $39 billion a year earlier. Analysts were expecting revenue of $44.85 billion. AT&T also lost 778,000 premium TV subscribers, a category that includes DirecTV satellite and U-verse television customers, much more than 544,000 losses in the first quarter.

**BHP Group PLC to invest US$400 million to fight climate change** - CEO Andrew Mackenzie has announced a range of new measures aimed at evolving BHP's response to climate change. Speaking in London, Mr. Mackenzie said BHP will:

- Establish a US$400 million Climate Investment Program to develop technologies to reduce emissions from our operations as well as those generated from the use of our resources.
- Establish a new medium-term, science-based target for scope one and two emissions in line with the Paris Agreement.
- Strengthen the link between executive remuneration and emissions performance from 2021.
- Develop a new climate portfolio analysis report in 2020 to evaluate the potential impacts of a broader range of scenarios and a transition to a "well below" two-degree world.

"We require a considered and orderly transition to a lower carbon world, in which resource companies like BHP have both critical expertise and a key role to play," Mr. Mackenzie said. "We must take a product stewardship role for emissions across our value chain. And commit to work with shippers, processors and users of our products to reduce scope three emissions."

**Compass Group PLC's** performance from April 1st to June 30th, 2019. Organic revenue growth was 6.3% in the third quarter (up 6.7% excluding the impact of Easter), principally driven by strong revenue growth in North America with improving performance in Rest of World. For the nine months to June 30, 2019 organic revenue grew 6.5%. The North American business reported organic revenue growth of 8.5% in the third quarter (8.7% excluding Easter) and 8.1% in the nine months to June 30, 2019. The margin in the nine months to June 30, 2019 was maintained. The Group invested around £100 million in the third quarter on bolt-on acquisitions mainly in Europe. The total invested in acquisitions in the nine months to June 30, 2019 was £470 million. On June 11th, Compass announced it had agreed to acquire Fazer Food Services for an enterprise value of approximately €475 million. The proposed acquisition requires European Commission competition approval, a process which may take several months. Compass has maintained a strong investment grade rating and target net debt to EBITDA of around 1.5x. Management expect full year organic growth at the top of the 4-6% range and therefore the margin is expected to be in line with the prior year.

**Total S.A.'s** Adjusted net income of $2.9 billion was in-line with the company-compiled consensus estimate. Net operating profit of $3.5 billion was 7% higher than estimates, driven mainly by higher than expected upstream and refining & chemicals performance, including some benefit from positive tax credit in refining & chemical in the quarter. Upstream production of 2,957 thousand boed was 5% ahead of forecast, up 9% year/year. It is estimated that upstream net income per barrel of $7.5/boe, down $3.3/boe year/year and compares to the $6/barrel (bl) fall in Brent oil price. Reported cash flow from operations of $6.3 billion was in-line with year ago levels with an implied build of working capital of $0.46 billion. Excluding working capital move, reported underlying cash flow of $6.7 billion was up 5% year/year. With organic capital expenditure (capex) of $3 billion and dividends payments of $3 billion, there was a positive FCF post capex and dividends of $0.7 billion. Adjusting for scrip, it is calculated organic cash breakeven of $46/bl, down $5/bl year/year and flat quarter/quarter. Net debt of $31 billion was up 4% quarter/quarter with gearing (net debt to capital) of 20.6% up 1 percentage point quarter/quarter. Total re-iterated 2019 guidance for production growth and organic capex guidance to be less than 9% and around $14 billion.

## Economic Conditions

**The International Monetary Fund** (IMF) has cut its growth forecasts for the global economy for this year and next. It predicts growth of 3.2% in 2019, down from its April forecast of 3.3%. Growth next year is set to pick up to 3.5% next year, although that is below its earlier forecast of 3.6%. Growth "remains subdued", the IMF says, and there is an urgent need to reduce trade and technology tensions. The Fund has raised its growth forecast for the U.K. this year to 1.3% from 1.2%. The revision for the U.K. reflects what the report calls a stronger-than-expected first three months of the year, boosted by pre-Brexit stockpiling. Next year, the report predicts 1.4% growth. The U.K. forecasts are based on an assumption of an orderly Brexit followed by a gradual transition to the new regime. As the report notes, what this will be remains highly uncertain. The IMF named a no-deal Brexit as one of the key risks to global economic growth. "The principal risk factor to the global economy is that adverse developments - including further U.S.-China tariffs, U.S. auto tariffs, or a no-deal Brexit - sap confidence, weaken investment, dislocate global supply chains, and severely slow global growth below the baseline," the Fund said. (Source: BBC)

**U.S.** – The advance reading of the **U.S. GDP** for the second quarter, at 2.1% annualized rate of growth, clocked-in ahead of the expectations calling for a 1.8% advance. The all-important U.S. consumer sector was also a key contributor in the quarter, improving by 4.3%, yet government investment has also added to growth, increasing by 5.0% in the quarter. Business investment subtracted from growth, being down 0.6% in the period, while housing continued to shrink. Not surprisingly given the current trade tensions, U.S. exports also retreated, by 5.1%, in the quarter.

**U.S. existing home sales** were down 1.7% in June, the biggest drop since March, and the first drop since then, to a 2-month low of 5.27 million units annualized. There was an upward revision to May—from 5.34 million to 5.36 million, initially, so that softened the blow a little. And both **singles** and **condo** sales were down. The weather probably played a role in the setback along with a shortage of mid-to-lower priced homes available for sale, according to the National Association of Realtors. Prices continued to climb; **median sales prices** are up over 4% year/year. On a regional basis, the decline was concentrated in the important-**South** (where sales account for about half of the country) and the **West**. There was an encouraging sign: **first-time home buyers** accounted for 35% of total sales, a share not seen since the spring of 2012. In summary the housing sector is struggling to break higher despite lower borrowing costs and steady income growth but compared to the Financial Crisis / Global Recession in 2009, steady'ish growth isn't that bad.

**U.S. Durable goods orders** soared 2.0% in June on a sharp upswing in aircraft bookings and strength in most other areas, notably machinery and autos. The 3.1% acceleration in the latter reduces concerns about fading auto sales, while the 2.4% leap in the former underscores the need to expand capacity and automate in the face of labour shortages and still sturdy consumer demand. **Core capital goods orders jumped 1.9%**, building on the prior month's 0.3% advance, and up for the fifth time this year. Nondefense capital goods shipments (including aircraft, which feeds into GDP) vaulted 1.5% after a 0.5% advance. **Core capital goods shipments excluding aircraft are on a solid upward trend**, rising 0.6% in June after a 0.5% advance in May and up in 5 of the past 6 months. The gains were widespread, including machinery. Businesses, though wary of tariffs, remain upbeat enough to expand capacity and spend on productivity-enhancing digital technologies.

**U.K.** - The next leader of the U.K. Conservative Party and de facto Prime Minister is Boris Johnson. He beat Jeremy Hunt with twice as many votes and succeeds Theresa May in trying to accomplish what she has not been able to do -- leave the EU. Johnson promises to take the U.K. out of the EU with or without a deal by October 31 and now has just 100 days to do it with upcoming summer break for Parliament in the calendar.

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## Financial Conditions

**The European Central Bank** (ECB) left rates unchanged, but in the press conference Mario Draghi, President of the ECB, sounded increasingly worried about the macro outlook, particularly for inflation, and signaled that the ECB will prepare a complex package of measures to address these concerns. Mr. Draghi also stated that if this macro deterioration continues fiscal policy will have to become the main lever rather than monetary policy. The question then for the next ECB meeting (on September 12) is in our opinion whether Mr. Draghi can pull off another "whatever it takes" moment, or whether the ECB is getting to the end of the line in terms of what it can do to support the Euro area economy.

The U.S. 2 year/10 year treasury spread is now 0.20% and the U.K.'s 2 year/10 year treasury spread is 0.20% - 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 costs of capital. Also, the narrowing gap between yields on the 2 year and 10 year Treasuries is of concern given its historical track record that when shorter term rates exceed longer dated ones, such inversion is usually an early warning of an economic slowdown.

Influenced by the withdrawal of quantitative easing, the U.S. 30 year mortgage market rate has increased to 3.75% (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 6.4 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 12.16 (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 bodes 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
- ITM AG Investment Trust
- Portland Advantage Plus - Everest Fund
- 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) per unit of our investment funds are published on our Portland website at www.portlandic.com/prices

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, 'GDP' gross domestic product, 'netback' is a measure of oil and gas sales revenues net of royalties, production and transportation expenses and is used to compare performance in the oil and gas industry, 'ROE' return on equity, 'ROTE' return on common equity, 'ROTCE' return on tangible common equity.



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