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PORTLAND INVESTMENT COUNSEL®

Our views on economic and other events and their expected impact on investments. February 27, 2017

Energy Sector

U.S. land rig count increased by 3 rigs week/week to 733 rigs, the first single-digit increase after five weeks of double-digit gains. The rig count is up on average 28% Quarter to date quarter/quarter. Gains in Horizontal Oil (+9) and Horizontal Gas (+1) were offset by declines in Vertical Oil (-4), Directional Gas (-2), and Directional Oil (-1) with Vertical Gas flat week/week. Total horizontal land rig count is down 55% since the peak in November 2014. The Permian currently makes up 52% of all oil rigs.

U.S. horizontal oil land rigs increased by 9 rigs week/week to 502, breaking the 500 mark for the first time since September 2015, as gains in the Permian (+5), Eagle Ford (+4), Woodford (+1), and "Other" (+1) were slightly offset by declines in Williston (-1) and Granite Wash (-1) as DJ-Niobrara and Mississippian remained flat week/week.

Canadian rig count increased by 9 rigs week/week and is up 97% from the level this time last year.

U.S. Gulf of Mexico offshore rig count remained flat week/week at 17 and is down 69% since June 2014.

Crescent Point Energy Corp. reported total average production in the fourth quarter of 165,097 barrels of oil equivalent per day (boed) down from 176,108 boed in the previous comparative period. But the company benefited from higher commodity prices as oil prices have recovered from a two-and-half-year slump. "2016 was a successful year," Chief Executive Scott Saxberg said in a conference call. "We exceeded our production targets on budget, increased drilling efficiencies and developed new plays." Crescent Point's average selling prices rose to C$49.32 per boe in the three months ended Dec. 31 from C$41.98 a year earlier. Saxberg said the company is interested in selling some "basic, simple, non-core assets" of a "smaller nature" to pay down debt or to free up funds for capital expenditure. "It'll be … anywhere from C$50 million ($38 million) to C$100 million kind of size," he said. Saxberg also said the company has never been approached by an activist investor, addressing a media report that said one had targeted Crescent Point.

Whitecap Resources Inc. achieved low-cost organic reserve additions and growth in 2016 after spending only $174 million of field capital (26% reduction compared with the previous year), which represented only 45% of its funds flow. Record low finding and development (F&D) costs of $2.34/boe, including changes in future development capital (FDC), resulted in a recycle ratio of 11.3x in 2016. Whitecap was also able to capitalize on the low crude oil price environment by transacting on $486.2 million (net) of strategic acquisitions. In aggregate, Whitecap invested $660.2 million (including acquisitions and net of divestments) into the development and expansion of its existing core areas growing total proved plus probable (2P) reserves by 28% or 13% per debt-adjusted share at a finding, development and acquisition (FD&A) cost of $11.51/boe, including changes in FDC, resulting in a recycle ratio of 2.3x.

Financial Sector

Ares Capital Corp. (ARCC) reported Q4 2016 core net investment income per share of $0.42 (which excludes roughly $0.01/share of costs related to the American Capital, Ltd. (ACAS) acquisition), better than the consensus of $0.39, with the beat driven primarily by higher dividend income of $22 million and structuring fees of $36 million. Book value per share was lower by ~1% quarter/quarter to $16.45, due to ~$0.20/share of net unrealized losses that were partially offset by ~$0.10/share of net realized gains. The recent closing of the ACAS deal should provide a longer-term runway for value creation, with roughly $1.3-1.5 billion of potential investment rotation available. The purchase of ACAS makes Ares by far the largest Business Development Corporation with approximately $12 billion in total assets post-close. A big focus remains the GE joint venture (senior security loan program or SSLP) and the potential impact on the returns in the SSLP. With the joint venture in wind down, all repayments in the SSLP go to pay-down the lower cost GE debt which reduces the returns to ARCC. This decreases the yield on the investment. The ACAS transaction helps this situation by making the SSLP a smaller percentage of their portfolio and also allows ARCC to ramp up its joint venture (SDLP) with Varagon (AIG) and reach critical size, offsetting the now lower returns from SSLP that is running off (slowly). Additionally, ARCC will be waiving fees for 10 quarters post-closing of ACAS which should help earnings during the implementation of ACAS's portfolio for the transaction and the wind-down of the SSLP. ARCC had $1.16 billion of new commitments during the 4th Quarter, of which approx. 57% were in first lien, 33% were in second lien securities, 7% were in subordinate certificates of the SDLP and 3% in other equity securities. Against that, ARCC had $1.1 billion of exits. The portfolio mix at quarter end was 23% first lien (vs. 25% previously), 34% second lien (vs. 32% previously), 22% in certificates of the SSLP (unchanged), and 3% in certificates of the SDLP (vs. 2% previously). Overall yield on debt and income producing securities fell to 9.4%, down from 9.7% last quarter. The yield of the SSLP was 7.0%, down from 8.5% last quarter. But the yield of the SDLP was 14% (up from 13.5% last quarter). Balance Sheet Leverage of approx 0.75x debt to equity, up from 0.71x the prior quarter. Non-accruals at amortized cost was 2.9%, modestly up from 2.3% last quarter.

Barclays PLC reported underlying Profit Before Tax of £284 million compared to consensus of £607 million with stronger income (+2%/£105 million vs. consensus) whilst costs were 11%/£432 million worse, impairment 19%/£104 million worse and other net income £108 million better. However, the headline numbers mask an underlying decent result in our view. The miss on costs was driven by £395 million of front loaded deferred compensation costs in the core. Whilst impairment was genuinely worse, other net income benefited from the recycling of foreign exchange translation following the Southern European cards business disposal. Excluding the cost impact and the foreign exchange recycling the core business looks to have been about 3% ahead of consensus. Capital was also a beat with Core Tier I at 12.4% (+0.6% versus consensus) leaving the group in their target range 12.3-12.7% with Tangible Net Asset Value in line at 290p and the group benefitting from lower deductions. Updated guidance on non-core business sees it being rolled back in to the group at 1st Half 2017 with £25 billion of Risk Weighted Assets at that point and a £1 billion expected loss for 2017 in line with expectations to complete the remaining wish to divest down to a minority stake in its Africa business from which deconsolidation provides additional strengthening of capital base, estimated at 0.75%. During the conference call concerns over the sustainability of the capital level centred on the accounting treatment of Barclays' UK pension scheme, which moved from a £1.1 billion deficit to a £27 million ($34 million) surplus in the last quarter of 2016. Capital has been a concern for investors since the Bank of England said last November that Barclays had fallen short of one of its targets in a stress test scenario, but stopped short of requiring the bank to submit a new plan to boost reserves. CEO Jes Staley's earlier determination to shape Barclays into a transatlantic bank now looks increasingly attractive in our view, i.e. post the Brexit decision and election of U.S. President Donald Trump – but it is still more of a wait and see story.

Berkshire Hathaway Inc. reported a higher quarterly profit though operating income fell. In his annual letter to Berkshire shareholders, Warren Buffett said investors "will almost certainly do well" by staying with the long term with a "collection of large, conservatively financed American businesses." Buffett puts Berkshire in that category, using the letter to tout the successes of many of his Omaha, Nebraska-based conglomerate's more than 90 operating units. These included businesses such as the BNSF railroad and Geico auto insurance that posted weaker results last quarter. For the fourth quarter, Berkshire's net income rose to $6.29 billion, or $3,823 per Class A share, from $5.48 billion, or $3,333 per share, a year earlier, helped by a $1.1 billion increase in gains from investments and derivatives. Operating profit fell 6% to $4.38 billion, or $2,665 per share, from $4.67 billion, or $2,843 per share. Analysts on average had forecast operating profit of $2,716.60 per share, according to Thomson Reuters. Book value per Class A share, reflecting assets minus liabilities and which Buffett calls a good measure of Berkshire's intrinsic worth, rose 11% to $172,108. For all of 2016, profit was virtually unchanged, dropping to $24.07 billion from $24.08 billion. Buffett said Berkshire still has about $86 billion of cash and equivalents, despite recent heavy spending on Apple and airline stocks.

Canadian Imperial Bank of Commerce (CIBC) reported adjusted cash EPS +13% year/year to $2.89, above consensus of $2.59. The beat primarily reflects stronger revenues driven by record trading and modestly lower Provisions for credit losses, partly offset by higher expenses. CIBC raised its quarterly dividend by $0.03 or 2%, the 9th increase in the past 10 quarters. Earnings by Segment: Capital Markets +50% year/year, Wealth +11%, and Canadian Retail +3% partly offset by a higher loss in Corporate. Adjusted Return On Equity: 20.1% (+1.1% bps year/year). Core Equity Tier 1 ratio of 11.9%, up from 11.3% in Q4 2016, driven by internal capital generation (+39 bps), share issuance (+15 bps), sale & lease back of branches (+15 bps), partly offset by increased Risk Weighted Assets and foreign exchange (-14 bps).

HSBC Holdings PLC - 2016 profit 62% down year/year to $7.1 billion. The British bank blamed slowing economic growth in its main markets of Hong Kong and the U.K. for the profit slide, as well as a $3.2 billion impairment of goodwill to its private banking unit in Europe, and the impact of the sale of its operations in Brazil. The bank also announced it would buy back an additional $1 billion of shares, adding to $2.5 billion of repurchases it made last year.

Royal Bank of Canada (RBC) adjusted cash EPS up 14% year/year to $1.87, above consensus $1.77. Overall, all segments outside of Insurance / Caribbean were better than our forecast and up from the prior year. The beat primarily reflects a better revenue top-line (+$0.09), and lower Provisions for Credit Losses (+$0.04) partly offset by slightly higher expenses (-$0.03). RBC raised its quarterly dividend by $0.04 or 5%. Earnings by Segment: Led by Investor & Treasury +50%, Wealth +42%, Capital Markets +16% and Canadian Banking +8% with Insurance +2% and Caribbean down 22%.RBC's Core Equity Tier 1 ratio was 11.0% up from 10.8% in Q4 2016. Operating Return On Equity: 16.7%.

Royal Bank of Scotland Group PLC (RBS) reported an operating loss before tax of £4,082 million for 2016 and an attributable loss of £6,955 million, which included litigation and conduct costs of £5,868 million, restructuring costs of £2,106 million, the final Dividend Access Share (DAS) dividend of £1,193 million and Capital Resolution disposal losses and impairments of £825 million. Restructuring costs included a £750 million provision in respect of the 17 February 2017 update on RBS's remaining State Aid obligation regarding Williams & Glyn. An operating loss before tax of £4,063 million and an attributable loss of £4,441 million were reported in Q4 2016. Across its Personal & Business Banking (PBB), Commercial & Private Banking (CPB) and NatWest Markets (NWM) franchises, RBS reported a £163 million, or 4%, increase in adjusted operating profits to £4,249 million for 2016, and an adjusted return on equity of 11.1%, compared with 11.2% in 2015. Q4 2016 adjusted operating profit of £848 million was £320 million, or 61%, higher than Q4 2015. In 2016, RBS delivered against all of its operating financial targets; PBB and CPB had combined income growth of 2%, adjusting for transfers, underpinned by 10% net lending growth, expenses have been reduced by around £1 billion for the third year in succession as

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the bank continues to focus on digital channels and on simplification of its processes, and Capital Resolution Risk Weighted Assets (RWAs) have reduced by a further £14.5 billion, or 30%, to £34.5 billion, with 80% of RWAs now relating to PBB, CPB and NatWest Markets compared with 72% at the end of 2015. RBS states it is committed to achieving its sub 50% cost:income ratio and 12% return on tangible equity targets by 2020. Common Equity Tier 1 ratio of 13.4% reduced by 210 basis points during 2016.

Activist Influenced Companies

Nomad Foods Limited – Leading frozen food brand, Birds Eye, has announced the launch of a new market-leading multi-million pound above-the-line campaign for its Coated Fish range, including new advertising (TVC) featuring Captain Birdseye, product quality improvements across the entire range and a packaging refresh. After almost a decade away from the nation's screens, Birds Eye is launching a new TVC for its Coated Fish range. Running across TV, VOD, out of home and social media, the campaign will reach over 25 million consumers and is designed to remind Brits of the great taste and quality of Birds Eye battered and breaded fish. 'The Coated Fish sector is currently worth over £200 million and as the leading brand in frozen, we want to drive category growth in 2017; offering great tasting, quality products, supported with unrivalled category media investment', said Adam Draper, Birds Eye UK General Marketing Manager. To further bolster the launch, new packaging will see the introduction of Captain Birdseye across the Coated Fish range to aid stand-out and find-time on fixture. The new packs will be in store from the end of February.

Canadian Dividend Payers

Northland Power Inc. reported fourth quarter and full year 2016 results which were ahead of the consensus expectations. Sales for the full year increased by 51% or $370.9 million and gross profit increased by 80.3% or $403.3 million, respectively over 2015. Adjusted earnings before interest, taxes, depreciation and amortization (EBITDA) increased by 55.9% or $224.8 million over 2015 to $626.9 million. Free cash flow per share was $1.40 in 2016 versus $1.09 in 2015, an increase of 28.5% from 2015. Net income was $190.6 million for the year compared to $27.5 million in 2015. All 150 wind turbines at the company's 600 MW, North Sea, Gemini wind farm are producing full power and have earned pre-completion revenues of €181.5 million (CAD $266.1 million) at the prescribed contract rate and price for 2016. Nordsee One, the company's 332 MW German wind farm, continues to progress on schedule and within budget. During 2016, all 54 foundation monopiles and transition pieces, along with the offshore substation and in-field cables, were successfully installed. In 2017, management expects adjusted EBITDA to be $660 to $710 million, an increase of approximately 9% over 2016 and free cash flow per share to be in the range of $1.10 to $1.25 per share compared to $1.40 per share in 2016.

Global Dividend Payers

ABB Ltd. at the beginning of February, ABB discovered significant financial irregularities in the South Korean subsidiary. Its treasurer is suspected of forging documentation & colluding with 3rd parties to steal from the company. The estimated impact on the previously reported unaudited FY16 results is approx. USD$100 million (pre-tax) with impact limited to South Korea only.

Pattern Energy Group Inc. announced the completion of its 184.6 megawatt (MW) Meikle Wind power project located in British Columbia, approximately 33 km north of Tumbler Ridge. "Meikle Wind is now the largest wind facility in British Columbia, increasing the installed wind power capacity in the province by 37%," said Mike Garland, CEO of Pattern Development. The Meikle Wind facility is utilizing 61 GE wind turbines and has the capacity to generate clean energy for up to 54,000 homes in the province. The facility has a 25-year power purchase agreement with BC Hydro. The 184.6 MW Meikle Wind facility expanded British Columbia's total installed wind capacity to 673.6 MW, according to the Canadian Wind Energy Association (CanWEA).

Walmart Stores, Inc reported adjusted quarter EPS of $1.30, in-line with consensus of $1.29. Comparisons at Walmart U.S. were the strongest since 2nd quarter 2013 at +1.8%, driven by traffic of 1.4% (excl. Jet.com). The comparisons may have benefitted from early seasonal markdowns, but nevertheless suggests that Walmart is gaining momentum and share. The outlook for 2018 remains as expected with EPS expected to be essentially flat relative to 2017 at the midpoint of guidance. Walmart comparisons will benefit from e-commerce growth and less cannibalization. 2018 operating margin will remain under pressure, we believe, given Walmart's e-commerce initiatives and price investments, but we believe Walmart is in the early stages of sustainably repositioning itself.

Economic Conditions

Canada – retail sales retreated 0.5% in December, offsetting a 0.3% in the prior month, with most retail categories suffering, including autos, clothing, furniture and electronics. Core retail sales, which excludes sales of vehicles and parts were also weaker than expected, down 0.3% compared to an expected 0.6% advance.

Headline inflation, as measured by changes in the consumer price index (CPI), jumped to 2.1% in January, ahead of the expectations for a more modest acceleration, to 1.6%. The core inflation reading, which excludes the effects of the most volatile price series, including food and energy, was up to 1.7%, one tenth ahead of December's reading.

U.S. existing home sales exceeded expectations. Sales jumped 3.3% (biggest monthly increase in over a year) in January to a decade-high (or February 2007) 5.69 million units annualized. Gains were spread around the country with the exception of the Midwest. More sales closed for **single-family homes** (+2.6% to a decade-high 5.04 million), as well as for **condos** (+8.3% to 0.65 million, the 2nd highest in a decade). Although more owners put their homes on the market at the start of the year, supplies are low. The **inventory of homes available for sale** now sits at just over 1.5 million units; over the past three decades, the average is 2.2 million units. But for the latest month, this translates into **3.6 months' supply**, which is pretty much a record. This is putting additional pressure on prices, with the **median sales price** rising over 7% from year-ago levels.

U.S. new home sales rose 3.7% in January to a 2-month high of 555,000 units annualized, following December's 7.0% dive. Still, this was disappointing in our view and it was accompanied by downward revisions to the prior three months. Three of the four regions across the country saw stronger sales….except for the West Coast, which was hit with plenty of snow and rain in the month. More homes were available for sale, but with the modest increase in sales, held the months' supply steady at 5.7, a 1½-year high but still below 'normal'. In other words, there is still a supply issue. That's putting more pressure on prices, which rose 7.5% from a year ago. And, it took a little less time to sell a home … from completion to the sign off.

U.S. Durable goods orders rose 1.8% in January, close to expectations, led by sharp gains in aircraft and defense spending. After three strong monthly gains, "core" capital goods orders (ex-aircraft and defense) slipped 0.4% on a pullback in computers and electrical equipment, though this measure is still up 10% annualized in the past three months. Machinery orders rose solidly for a fifth straight month, likely reflecting an upswing in business capital expenditure.

U.K. economy grew by more than previously reported in the final three months of 2016, according to the latest official estimate. Gross Domestic Product (GDP) increased by 0.7%, up from 0.6%, according to the Office for National Statistics (ONS). The upward revision is mainly due to manufacturing industry having done better than thought. The ONS cut its estimate for growth in 2016 as a whole to 1.8%, down from the 2% it forecast last month. (Source: BBC)

Financial Conditions

The U.S. 2 year/10 year treasury spread is now 1.17% and the U.K.'s 2 year/10 year treasury spread is 1.06% - 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.

Influenced by the withdrawal of quantitative easing, the U.S. 30 year mortgage market rate has increased to 4.16% (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 11.90 (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 Focused Plus Fund
- Portland Private Income Fund
- Portland Global Energy Efficiency and Renewable Energy Fund LP
- Portland Advantage Plus Funds
- Portland Private Growth Fund
- Portland Global Aristocrats Plus Fund

Individual Discretionary Managed Account Models - SMA

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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