News Highlights

Owners. Operators. And Insightful Investors.

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PORTLAND INVESTMENT COUNSEL®

Established in 2007

Our views on economic and other events and their expected impact on investments. April 22, 2019

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Owner Operated Companies

BlackRock Capital Investment Corporation, the world's largest asset manager, reported first-quarter profit that exceeded expectations and took in $65 billion of new investor cash as global financial markets rebounded from a volatile fourth quarter. Total assets under management grew 3% to $6.52 trillion in the quarter through March 31 from a year earlier, amid a broad-based rebound in global equity markets. Assets had dipped below $6 trillion amid market turmoil late last year. Overall, the company sold $59 billion in stock, bond and other "long-term" investment funds, up from the $43.6 billion in the quarter ended December 31. BlackRock lost more than $26 billion in its equity portfolio during the first quarter, but this was more than offset by a jump in fixed income of nearly $80 billion. Net income attributable to BlackRock fell to $1.05 billion, or $6.61 per share, in the first quarter, from $1.09 billion, or $6.68 per share, a year earlier. Nonetheless, that result exceeded analysts' expectations for a profit of $6.13 per share, according to data from Refinitiv US Holdings, Inc.

Danaher Corporation announced results for the first quarter 2019 which included net earnings of $333.8 million, or $0.46 per diluted share which represented a 41.0% year/year decrease from the comparable 2018 period. Non-GAAP adjusted diluted net earnings per share were $1.07, which represents an 8.0% increase over the comparable 2018 period. For the first quarter 2019, revenues increased 4.0% year/year to $4.9 billion, with non-GAAP core revenue growth of 5.5%. For the full year 2019, Danaher now anticipates that diluted net earnings per share will be in the range of $3.34 to $3.42 versus previous guidance of $3.85 to $3.95. The company now expects its 2019 non-GAAP adjusted diluted net earnings per share to be in the range of $4.72 to $4.80 versus previous guidance of $4.75 to $4.85. This updated guidance reflects the dilution related to Danaher's recent equity offerings to fund the General Electric Company's (GE) Biopharmaceutical acquisition, partially offset by the company's first quarter 2019 performance. Thomas P. Joyce, Jr., President and Chief Executive Officer, stated, "During the first quarter, we achieved 5.5% core revenue growth and believe we expanded our market-leading positions across a number of our businesses. Combined with high-single digit adjusted earnings per share growth and good cash flow generation, our performance is a testament to our team's focused execution and the power of the Danaher Business System." Joyce continued, "We are excited about our recently announced agreement to acquire GE Biopharma and continue to expect the deal to close in the fourth quarter of this year. The business will be an excellent complement to our current biologics workflow solutions and will bring a highly innovative, industry-leading product suite to our Life Sciences portfolio. We look forward to welcoming this talented team to Danaher."

Energy Sector

Canadian Association of Petroleum Producers Symposium – We had the opportunity to reconnect with the management teams of some of our key energy holdings, including Crescent Point Energy Corp., Baytex Energy Corp. and Whitecap Resources, Inc., during the two-day Canadian Association of Petroleum Producers (CAPP) Energy Symposium. The central theme of the conference was the increased availability of FCF to oil and gas operators in Western Canada. This is in part a consequence of a stronger commodity environment and in part because, much like their peers South of the border, Canadian producers seemed to have received the message from the investment community that they should focus more on profitability and less on production growth. Most companies present emphasized the need to strengthen their balance sheet and, as such, have repayment of debt as a first call on the excess cash flows. The goal of most companies is to reach a level of indebtedness, which would make the operations sustainable through a potential commodity downturn and crude oil prices in low $40/barrel (bbl) for West Texas Intermediate (WTI), the North American benchmark. Whitecap Resources is also indicating that an upward revision of its dividend level is quite likely at its next annual general meeting later this month, as the company sees itself able to sustain current payouts even in a mid to high $30/bbl commodity environment, when accounting for the commodity and price differential hedges the company has in place. The energy companies our funds invest in have taken active measures to hedge their production in this improving commodity environment, as well as to protect themselves against exit issues scenarios, such as the one which unfolded in the last quarter of 2018. Much of the production by the companies held in our funds are not subject to the egress concerns, as it is either situated downstream of the current bottlenecks or geographically dispersed, including in Eagle Ford (Texas), Uinta (Utah) and Saskatchewan. Crescent Point is actively pursuing a number of divestitures, including light and medium oil non-core assets and field gas gathering and processing infrastructure, with the goal of using the proceeds to primarily reduce corporate indebtedness. Crescent Point has undergone major corporate governance changes over the past couple of years, with thoroughly renewed board roster and key top management changes. Baytex Energy is also wrapping up its own corporate structure changes as the result of its merger with Raging River, last year and is emerging as a more diversified, lower leverage core North American energy producers. The company is seeing improved productivity in its prolific Eagle Ford acreage and has started to delineate its highly prospective East Shale Duvernay land. Other key areas of interest at the conference were developments in oil field services, a more acute awareness of environmental, social and governance (ESG) issues in the age of 'fossil fuel divestiture' and an overall more upbeat outlook, partly driven by the result of the Alberta provincial elections.

Financial Sector

Bank of America Corporation posted Q1 2019 EPS of $0.70. Consensus was $0.67. Results included Debt Value Add losses of $90 million ($0.01). Both Q1 2018 and Q1 2019 included a $0.2 billion ($0.02) tax benefit related to stock-based compensation. Its loan loss provision was $22 million greater than net charge-offs ($19 million reserve release last quarter). Operating revenues were little changed year/year and increased 2% linked quarter to $23.2 billion. Tangible book increased 2.0% to $18.26 (trading at 1.6x). It posted an 11.42% ROE and 16.01% ROTCE. Its CET 1 ratio was 11.6%. It repurchased $6.3 billion in common stock. Average diluted shares declined by 2.1%. Average earning assets increased 1.2%. Its net interest margin declined 1 basis point (bps) to 2.51%. Excluding Global Market, its Net Interest Margin was unchanged at 3.03%. Its yield on average earning assets increased 8bps to 3.68%. Expenses declined 4% year/year as efficiency savings, lower insurance costs and lower amortization of intangibles were partially offset by investments. Its cost/income efficiency ratio was 57.5%. It produced its 17th consecutive quarter of positive operating leverage. Its tax rate was 16.6%. Its reserve/loan ratio was unchanged at 1.02%.

The Goldman Sachs Group Inc. reported Q1 2019 EPS of $5.71 and consensus was $4.96. Results included provisions for litigation and regulatory of $37 million ($0.08). Revenues fell 13% year/year (more robust market backdrop in Q1 2018) and increased 9% sequentially (aided by seasonality). Institutional and Corporate Services fell 18% year/year (Fixed Income Currency & Commodities -11%, equities -24%), Lending declined 14% (though Net Interest Income +50%), Investment Management decreased 12% (though management fees were little changed), and Investment Banking was relatively stable (advisory up, underwriting lower). While revenues were challenged compared to a solid Q1 2018, it noted activity level certainly improved meaningfully in the second half of the quarter. Near-term, analysts expect results to benefit from a solid initial public offering pipeline and continued mergers & acquisitions activity. Goldman still managed to produce a 12% ROTCE. While commentary on 1MDB (Malaysia Development Bank) was limited, analysts believe consensus is forming in the $2-$5 billion area for a possible settlement.

Morgan Stanley reported Q1 2019 EPS of $1.39. Consensus was $1.17. The quarter included intermittent net discrete tax benefits of $101 million ($0.06) putting core EPS closer to $1.33. Relative to consensus, better than expected Fixed Income, Currency and Commodities trading (client structuring activity, credit), wealth management (transactional, other) and investment management (investment gains) revenues drove the upside. Still, investment banking fees (outperformed peers in equity underwriting but lagged in debt underwriting and advisory) and equity trading revenues (though approximated peers) were light. Revenues fell 7% from a record Q1 2018 and increased 20% linked quarter to $10.3 billion. Relative to Q1 2018, revenues in Europe Middle East & Africa were unchanged, while Americas (-9%) and Asia (-7%) declined. Tangible book increased 1.7% to $37.62 (trading at 1.25x). It posted a ROE of 13.1% and ROTCE of 14.9%. Its CET 1 ratio was 16.5% (-40bps). Total assets increased 3% linked quarters, while Risk Weighted Assets rose 4% or $15.5 billion. During the quarter, it repurchased $1.2 billion of its common stock, approximating Q3 2018's and Q4 2018's pace. It has now repurchased roughly three-quarters its $4.7 billion Capital adequacy 2018 allowance. Average diluted shares declined by 1.6%.

Activist Influenced Companies

Brookfield Business Partners L.P. – North American Palladium Ltd. and the majority shareholder of the company, an affiliate of Brookfield Business Partners, a publicly listed business services and industrials company of Brookfield Asset Management Inc. have announced that the previously announced offering of 5,770,000 common shares has closed. As a result of the offering, Brookfield's ownership interest in the Company has been reduced from approximately 90.85% prior to the Offering to approximately 81.05% (Brookfield now holds 47,689,128 common shares). The net proceeds of the offering will be paid directly to the selling shareholder.

Dividend Payers

Barrick Gold Corporation reported Q1 2019 sales of 1.37 million ounces (Moz) gold as strong attributable production from Barrick Nevada, Hemlo and Kibali was partially offset by a soft quarter at Kalgoorlie where last year's pit wall slide appears to be continually impacting production. Copper production was 106 million pounds (Mlb) in the quarter, down 3% from the prior quarter (109Mlb) but ahead of estimates. Jabal Sayid had record production in the quarter. Production was 1.36Moz gold and 106Mlb copper. Barrick will report Q1 2019 earnings pre-market on May 8. This will be the first quarterly report for Barrick-Randgold Resources Ltd. Expectations are for: 1) gold cash costs of $668/oz net of by-products and copper cash costs of $1.80/lb net of by-products; 2) operating cash flow of $576 million and capital expenditures of $369 million resulting in FCF of $208 million and a quarter-end net debt position of $4.09 billion; 3) updates on the combination of the two companies and mineral resource management efforts including exploration results and thoughts on potential asset disposals and evaluations of strategic assets.

BHP Group PLC delivered another weak set of production numbers in Q3, cutting the guidance range for iron ore by 8-13 million tonnes (100% basis) on the back of cyclones in March to a level 3% below analysts' forecast. The resulting 7% increase in unit cost guidance will also put pressure on estimates although clearly this is being more than offset by iron ore prices (+13% since end of March). Elsewhere production guidance was unchanged – oil looks set to beat guidance (10% decline quarter/quarter in Q4 to meet top end), copper is tracking in line and coal looks weak with both met and thermal likely to miss the bottom end of guidance in analysts' view (29% and 18% quarter/quarter growth required to hit bottom end respectively).

Bunzl PLC - Organic growth in the first quarter was 1.5%, which was below estimates. The lower growth is a result of weaker GDP growth generally across the group's regions and lower sales to the grocery and retail segments in North America. We think it represents an approximately 4% reduction to full year EPS, before foreign exchange and additional acquisitions. North America weakness – Sales to grocery and retail customers have seen a mild sales decline (between 0% and 1%) as a result of input cost inflation flattening out and no net volume growth. The customers themselves aren't growing and, after a strong period of Bunzl winning new outsourcing work, this period has no big new wins. Rest of the World also seeing slower growth - Underlying growth in the rest of the group was approximately 2%, which is being attributed simply to slightly weaker GDP growth across the regions. This could certainly apply to the key markets of Europe, the U.K. and Australia. Lower growth has margin implications due to fixed costs. If you reduced growth by 1.5% analysts' believe it would have an approx. 2-3% impact on EBITA and 3-4% on EPS. One small new acquisition has been announced and management believe the pipeline is still good.

Economic Conditions

China's GDP grew 6.4% year/year in Q1 2019, above consensus forecast of 6.3%. Nonetheless, the quarter/quarter seasonally adjusted growth eased to 1.4% in Q1 2019 from 1.5% in the preceding quarter. Meanwhile, the monthly economic indicators in March that were released last week continued to corroborate earlier releases of the export and Purchasing Managers Index data to show signs of green shoots in the Chinese economy. Despite the set of stronger economic data in March, the recovery in the Chinese economy remains tentative at this point until analysts have further data confirmation: 1) the recovery in March economic indicators (in particular the exports) could be mainly due to seasonal factors as business resumed post Lunar New Year holidays; 2) recovery in export and industrial activities remain vulnerable to global trade tensions (not limited to U.S.-China); and 3) demand from developed economies could still turn out to be weaker-than-expected.

U.K. Wage growth at decade high - According to the latest Office for National Statistics, labour conditions within the jobs market remained tight with employment growing by 179,000 in the three months to February. This helped to keep the unemployment rate at 3.9%, its lowest since early 1975. Contrasting with other sluggish economic readings, average earnings (including bonuses) rose by an annual 3.5% year/year in the three months to February, the fastest pace in over a decade as employers extended their hiring spree. Excluding bonuses, average weekly earnings increased by 3.4% year/year. Wage growth continues to outpace inflation.

Japan's exports contracted for a fourth straight month by -2.4% year/year in March (from -1.2% in February), quite in line with Bloomberg's median forecast of -2.6%. This is the longest stretch of monthly export decline recorded since December 2016. Imports rebounded with a 1.1% year/year increase in March (from -6.6% year/year in February), although the pace was less strong than Bloomberg's median forecast of +2.8%. Even though exports came in weak, it was coupled with a benign import rebound, resulting in wider than expected trade surplus of JPY 528.5 billion in March (from a more modest JPY 334.9 billion surplus in February and above Bloomberg's median expectations for a smaller surplus of JPY 363.2 billion). On a seasonally-adjusted basis, the trade balance turned into a deficit of JPY 177.8 billion, from a surplus of JPY 116.1 billion in February.

Australian employment grew strongly in March, rising by 25,700 during the month, close to double the 15,000 increase expected. Full time employment climbed by 48,300, more than offsetting a 22,600 decline in part time workers. The unemployment rate rose to 5.0% after seasonal adjustments, up 0.1% from February. A lift in labour force participation to 65.7%, up from 65.6% in February, explained the lift in unemployment, reflecting that the size of Australia's labour market grew faster than employment growth during the month.

Financial Conditions

The U.S. 2 year/10 year treasury spread is now 0.19% and the U.K.'s 2 year/10 year treasury spread is 0.43% - 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 4.17% (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 3.9 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 13.31 (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.

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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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