



News Highlights

Financial Services Companies

Barclays - Trading in Barclays' "dark pool" fell more than a third in the wake of the lawsuit brought by the New York State Attorney General alleging the bank misled investors about the presence of high frequency traders. The decline took Barclays from being the second largest dark pool operator in the US by market share to fifth place. Credit Suisse maintained its top spot, according to the Finra data, while UBS was second and Deutsche Bank third in the latest week.

Bank of America : GAAP EPS was \$0.19 and included litigation expense of \$4.0B pre-tax (or \$0.22 per share). Ex-legal, adjusted ex-release EPS looks to be somewhere in the low-\$0.30s. Just as an example, if we take out all reserve release, knock out \$700mm from the strong fee results, use a 30% tax rate, and use \$14.5B ex-legal costs, adjusted EPS would be around \$0.33. Investment -banking fees increased \$0.1B Q-Q to \$1.7B, as equity underwriting was stronger but advisory and debt underwriting revenues were slightly lower. Total core trading declined only 1% Year-on-Year, which is better than peers (Citi down 15% and JPM down 14%). Overall, firm-wide revenues of \$22.0B (vs. \$22.8B in 1Q) were ok, particularly Investment-banking and trading revenues, equity investment income, gains on debt securities, and "other" fees. Most other revenue lines were in-line with expectations. Net interest income (NII) decreased \$0.1B Q-Q to \$10.2B and the reported Net Interest Margin fell 7bp to 2.22% (core NIM ex. market-related adjustments down 10bp). Lower market-related NII was a \$0.2B drag vs. the \$0.3B drag last quarter. Loan balances were disappointing, with balances down modestly (down 0.5% Q-Q) as the discretionary mortgage portfolio continues to decline and Commercial Real Estate saw continued net pay-downs. Core expenses [ex. litigation, Legacy Asset Servicing (LAS), and 1Q retirement eligible comp costs] were \$13.1B in 2Q vs. \$13.6B last quarter. This is a good result considering I-banking and trading revenues were better than expected. We note that Bank of America now expects to achieve quarterly 'New Bank of America' cost saves of \$2.0B by 4Q14 (vs. mid-'15 previously), but quarterly LAS expense is now expected to decline to \$1.1B by 1Q15 (vs. 4Q14 previously). Provision expense was lower-than-expected at \$411mm (vs. \$1,009mm last quarter). Reserve release was bigger (\$662mm in 2Q vs. \$379mm in

1Q), but charge-offs were also much lower (\$1,073mm vs. \$1,388mm last quarter). Net charge-off improvement was driven by residential real estate categories. The Basel III Tier 1 common equity capital ratio ended the quarter at 9.5% (up 50bp vs. 1Q), and the holding company Supplemental Leverage Ratio (SLR) is estimated to be above the 5% proposed minimum. Tangible book value was \$14.24 vs. \$13.81 last quarter.

First National Financial: announced that it has entered into an agreement with TD Bank to provide underwriting and fulfillment processing services for mortgages originated by TD through the residential mortgage broker channel. The company will use its underwriting platform (MERLIN) to accept mortgage applications from the TD mortgage broker channel and underwrite these mortgages in accordance with TD's credit policies, compliance standards and controls. TD will fund all the mortgages underwritten under the agreement and retain full responsibility for underwriting guidelines, mortgage servicing and the client relationship. We believe TD has about a 10% share of the mortgage broker channel, generating \$6-7 billion of mortgages through it annually. We view this agreement as positive for First National. Although the short-term impact is unlikely to be material (less than 5% of revenue), this is the first such deal that we are aware of. It demonstrates confidence in First National's underwriting platform and ability, and serves as a base from which it may win more deals with other large financial institutions in the future.

Goldman Sachs reported a headline EPS of \$4.10, well ahead of consensus \$3.09. The beat is driven primarily by the Investing and Lending division (2.07B vs 1.33B est), while Inv. Mgmt was more or less in line. Investment banking posted a modest beat as well, and Goldman Sachs talked about a decent pipeline. Equity Capital Markets and Debt Capital Markets were both better than expected, while M&A was a slight miss to our number. FICC trading and equity trading were both modestly better than expected forecast. Total expenses were slightly higher driven by higher comp. The tax rate of 30% was lower than the 33% forecast and accounted for 12c of the beat. Net income climbed 5% to US\$2.04bn, from US\$1.93bn, a year earlier. CEO Lloyd C. Blankfein pledged not to overreact to a trading slump that's now in its fifth year as he positions the firm to pick up market share from other banks that are pulling back. Blankfein is also relying on underwriting stocks and bonds, which accounted for 14% of revenue in the second quarter, the highest portion since 2000.



JPMorgan posted second-quarter profit that beat estimates as fixed-income trading revenue fell less than analysts expected. Net income declined 7.9% to US\$5.99bn, from \$US6.5bn a year earlier. JPM reported \$1.46, well above consensus of \$1.29. This appears to be a strong beat on quality earnings as we arrive at a core \$1.43 result after adjusting for Mortgage Service Rights net benefit (\$0.06), Debt Value Adjust gain (\$0.02), litigation expense (\$0.13), and reserve release (\$0.08). The Corporate and Investment Bank was the star of 2Q, with core revenues of \$8.9bn vs expectations of \$8.3bn. Investment Bank revenues were \$1.8bn vs \$1.6bn estimate, with better-than-expected results across the board but especially in Equity Capital Markets. Fixed Income, Currency and Commodities came in at \$3.5bn, beating estimates of \$3.1bn and down from \$4.1bn in the year-ago quarter. Equities of \$1.2bn were in line with estimates. Net Interest Income ticked up +1% QoQ. As a result, core profitability improved QoQ with Return on Capital Employed of 14.3% (from 14%). Non Conforming Obligations declined 9% QoQ. Coupled with a 3% decline in QoQ Non Performing Loans, provision expense of \$692mn declined 19% QoQ. As a result, reserve release of \$0.08beat expectations. The Basel III Tier 1 common ratio increased 20bp Q-Q to 9.8% (vs. the 10%+ target by YE14) and there was again good progress on the Supplemental Leverage Ratio (SLR), which increased to 5.4% (vs. 5.1% last quarter) at the firm-level and 5.6% at the bank (vs. 5.3%). Tangible book value was up 3.4% to \$43.17 and the bank repurchased 25mm shares (or \$1.4B in aggregate) (\$5bn left for 3Q14-1Q15).

Morgan Stanley reported 2Q14 EPS from continuing operations of \$0.94. Excluding Debt Value Adjustments of \$87mn, it was \$0.91. Results also included a net discrete tax benefit of \$609mn (\$0.31), principally related to the re-measurement of reserves and related interest. Ex. DVA and this tax benefit, EPS was \$0.60. Consensus was \$0.56. Higher than expected Investment Banking fees was the main driver of the upside. While it reported an ROE of 11.5%, excluding the tax benefit it was closer to 8%. Tangible book increased 4% to \$28.53. Its Basel III Common Equity Tier 1 ratio was 13.8%. Assets declined 1%, though Risk Weighted Assets increased 6%. Deposits rose 1%, while its global liquidity reserve decreased 5%. During the quarter, it repurchased \$284mn (28% of its CCAR 2014 ask) of its common stock or 9.3mn shares. Its average diluted share count was unchanged. Relative to 1Q14, revenues increased in Wealth Management (+3%) and declined Institutional Securities (-8%) and Investment Management

(-6%). By region, relative to 1Q14, revenues increased in EMEA (+5%) and declined in the Americas (-6%) and Asia (-1%). Results included a \$14mn benefit related to an insurance recovery. Expenses fell 2% y-o-y and were relatively stable with the prior quarter. Ex. DVA its comp ratio increased slightly from 48.9% to 49.3%.

Institutional Securities : Ex. DVA pre-tax income rose 15% y-o-y and declined 26% from 1Q14 to \$927mn. Revenue ex DVA declined 1% y-o-y and dropped 8% from 1Q14 to \$4.2bn. Investment banking fee increased 26% from 1Q14 to \$1.4bn, with increases in debt underwriting (+55%), equity underwriting (+8%) and advisory (+24%). Total trading revenues (ev. DVA) fell 5% y-o-y. Fixed Income, Currency and Commodities decreased 12% y-o-y and dropped 39% from 1Q14 to \$1.0bn. Wealth Management - Pre-tax income rose 17% y-o-y and gained 11% from 1Q14 to \$767mn. Revenues rose 5% y-o-y and increased 3% sequentially. Expenses rose 1% from 1Q14, driven by comp, though its comp/revenue ratio decreased from 60% to 59%, while its pre-tax margin rose from 19% to 21%. Clients assets rose 3% from the prior quarter to a record \$2.0trn. Investment Management - Pre-tax income increased 28% y-o-y but fell 22% from 1Q14 to \$205mn. Revenues rose 3% y-o-y and declined 6% from the prior quarter to \$692mn. Assets under supervision increased 4% to \$396bn. Total net flows were \$7.6bn, up from \$6.0bn in 1Q14.

Nordea : PBT €35m +6% (+€1m) ahead of consensus expectations. Revenue was down a bit (-2% on Q1 and -2% light against consensus) but more than offset by better costs (€1.4bn, 6% or €6m lower than consensus). Costs are +12% (€49m) up on Q1 but include a €90m restructuring charge (expected). Divisional performance includes better than expected Wealth (Rev +5% on Q2) and Centrals offset by weak Wholesale Banking (weak revenue -3% on Q2). Retail banking was in line (weak rev and better costs - better Sweden and Denmark / worse Norway). Core Tier 1 equity was 15.2% slightly better than 15.0% forecast (RWAs -4% on period). Management re-iterate ambition to increase payout ratio in 2014.

Ukraine and Russia and Nordea: Increasing tension between Ukraine and Russia, following the Malaysia Airline jet crash in Eastern Ukraine last Thursday, is adding even more uncertainty to an already complex situation. There are obviously bigger



issues, beyond financial impacts, at stake with this tragedy, and there are numerous issues that cannot be quantified, but of the European banks we invest in only Nordea has a presence in Ukraine and Russia, as % of total loans - Russian / Ukraine loans represent 1.7% of Nordea's total loan book which as % of tangible equity - Russian / Ukraine loans represents 21% of Nordea's tangible book value.

Dividend Payers

Barrick Gold announced that CEO/President Jamie Sokalsky will be stepping down effective Sept 15, 2014. Kelvin Dushnisky (Corp. and Gov't Affairs) and Jim Gowans (COO) become Co-Presidents. Ammar Al-Joundi (CFO) and Darian Rich (VP HR) were promoted to EVP. ABX believes the shared leadership role reflects the interconnected nature of operations and stakeholder relations and that the changes will divert more power to key management personnel.

GEA Group – the Dusseldorf-based engineering group received various major orders from the dairy processing industry in the second quarter of 2014. The orders, under which GEA will in particular be supplying and installing equipment for the production of dairy powder, total more than €60 million and were placed by customers in North America and Western Europe. The orders will mainly be executed in 2015 and 2016.

Johnson & Johnson – reported higher-than-expected quarterly results on very strong sales of its new Olysio treatment for hepatitis C, but company officials cautioned sales of the pill will slow down later this year as newer rivals come to market. Global company sales jumped 9.1% in the second quarter to \$19.5 billion, beating Wall Street expectations of \$18.99 billion. J&J only slightly boosted its full-year earnings forecast despite its outsized second quarter results, to between \$5.85 and \$5.92 per share - from its earlier outlook of \$5.80 to \$5.90. The diversified healthcare company said it had earned \$4.33 billion, or \$1.51 per share, in the second quarter. That compared with \$3.83 billion, or \$1.33 per share, a year earlier. Global company pharmaceutical sales surged 21% in the quarter to \$8.5 billion, with U.S. sales surging almost 37% - fueled by demand for Olysio, blood clot preventer Xarelto and prostate cancer treatment Zytiga. Sales of the company's wide array of medical devices and diagnostics languished, by comparison,

edging up 0.7% to \$7.2 billion. Consumer products, including over-the-counter medicines such as painkiller Tylenol, also put on modest performance, with sales rising 2.4% to \$3.7 billion.

Novartis – Swiss drugmaker posted a quarterly rise in sales that missed expectations and said it would focus on eking out gradual cost savings to boost margins as it prepares a radical business overhaul. Despite the sales miss, the Basel-based company confirmed its full-year guidance for a rise in sales and profit, expecting revenue from new products to offset generic competition to its blood pressure pill Diovan. Novartis unveiled a series of deals worth more than \$25 billion in April to get out of underperforming businesses such as vaccines and animal health operations while adding higher-margin cancer drugs from GlaxoSmithKline. Weak performance from the outgoing vaccines and animal health businesses weighed on second-quarter group sales that were up 2% at \$14.64 billion, slightly short of the average forecast of \$14.72 billion in a Reuters poll. Under the new structure, Novartis will concentrate on three “powerhouse divisions” - pharmaceuticals, its Alcon eyecare unit and generics division Sandoz - hoping a focus on a smaller number of leading businesses will help to drive growth as healthcare budgets come under pressure. It is also consolidating some back-office functions into a single shared-service organisation. These operations are currently spread across all divisions and account for more than \$6 billion in expenses. Novartis confirmed its full-year guidance for sales to grow in the low-to-mid-single digit percentage range this year as it braces for generic competition to lop \$2.7 billion off its top line. Core second-quarter operating income of \$3.8 billion fell slightly shy of the \$3.83 billion analyst consensus.

Novartis made two announcements last week: (i) Smart lens technology licensed in from Google for all medical uses: the agreement with Google provides Alcon with the opportunity to develop and commercialise Google's ‘smart lens’ technology with the potential to transform eye care and enhance Alcon's pipeline and global leadership in contact lenses and intraocular lenses: Novartis's interest in this technology is currently focused in two areas: Helping diabetic patients manage their disease by providing a continuous, minimally invasive measurement of the body's glucose levels via a ‘smart contact lens’ which is designed to measure tear fluid in the eye and connects wirelessly with a mobile device and; for people living with presbyopia who can no longer read without glasses, the ‘smart lens’ has the potential to provide accommodative vision correction to help restore the eye's natural autofocus on near



objects in the form of an accommodative contact lens or intraocular lens as part of the refractive cataract treatment. Given Alcon's leading role in the market of contact lenses, we believe it was a smart move on Google's side to team up with this Novartis division to innovate this market by marrying microchip-based technology with that of a contact lens as a carrier. First prototypes are expected to hit the market by 2015 but commercialized products are only expected in about 5 years. Novartis sees ophthalmology as one of the key growth driver for the company and smart contact lenses could support the growth case particularly with solutions for diabetics or automatic adjustments to individual sight.

(2) Collaboration with Banner Alzheimer's Institute on a clinical study in Alzheimer's disease. The study will determine whether two Novartis investigational anti-amyloid treatments (an anti-Abeta vaccine candidate and an oral BACE-inhibitor) can prevent or delay the emergence of symptoms of AD in people identified as being at genetic risk for developing the late-onset form of the disease. Nevertheless, it will take Novartis a few years before outcomes are recorded leaving Roche in a leading role.

Pacific Rubiales : announced last week that pilot tests on its STAR technology (Synchronized Thermal Additional Recovery) designed to extract heavy crude more efficiently, has been successful. It is yet to be evaluated by its Colombian partner, Ecopetrol.

Tesco – is to let go chief executive Philip Clarke and replace him with a turnaround specialist from Unilever, ending a disappointing three year reign as Britain's biggest retailer warned it would again miss profit forecasts. Clarke, who has spent more than £1 billion (\$1.7 billion) on a failed recovery plan in Tesco's main home market, will be succeeded on Oct. 1 by Dave Lewis, who is credited with revamping a succession of businesses at the consumer goods group and is currently its global president of personal care. Tesco has recently been squeezed between discounters Aldi and Lidl at one end and upmarket grocers such as Waitrose at the other, and hurt by the slowest growth in the overall UK grocery sector for over a decade. Clarke, a 40-year Tesco veteran who started as a teenager stacking shelves in a store managed by his father, fought back with a wide-ranging plan including trimming prices as well as revamping stores and product ranges, but the firm's market share and share price have continued to decline. Dave Lewis was chairman of Unilever UK and Ireland from 2007 until 2010, when he became president of the Americas. He took on his latest role

as head of personal care products in 2011. Lewis will work alongside new Tesco finance chief Alan Stewart, who quit Marks & Spencer MKS. Earlier this month but may not start at Tesco for six months due to a non-compete clause in his contract.

Tesco said trading had turned tougher than expected at the time of its first-quarter update on June 4, and that sales and trading profit in its fiscal first half were below expectations. Clarke, said on Monday he would "provide support" to Lewis until January 2015.

Economic Activity, Consumer and Business Conditions

US –retail sales grew by 0.25% in June, slower than the expected 0.60% advance, with auto sales pulling back 0.3% in the month, despite upbeat reports from the automakers. Retail sales excluding autos were up 0.4%, just shy of the expected 0.5% improvement, as growth in general merchandise, health and personal care and clothing categories was offset by a slowdown in sales of building and garden, furniture and food services categories. The preliminary reading of the consumer sentiment for July, by the University of Michigan, at 81.3 index points was lower than the expected 83.0 points level and roughly in line with June's 81.2 reading. The 'current conditions' component of the composite index actually advanced to a 97.1 level, a notch above expectation, while the 'expectations' component unexpectedly dropped to a 71.1 index points reading from June's 72.2 points level and short of the expected increase to a 74.0 points reading.

US industrial production had a more muted 0.22% rate of growth in June, short of the expected 0.4%, dragged lower by a 0.3% reduction in production of motor vehicles and parts, as well as a similarly sized pull-back in the utilities' output. The US capacity utilization inched lower to a 79.09% level in June from May's 79.13% reading. The US leading economic indicators (LEI), though improving by 0.29% in June, did so at a slower pace than the expected 0.5% advance and May's 0.69% reading, indicating continued growth in US business activity, though at a slower pace than earlier believed.

The US home builders have once again turned 'optimistic'. The National Association of Home Builders' (NAHB)



housing market index unexpectedly jumped to 53 index points, re-entering the 50+ 'optimistic' range which it left in February, helped by a jump in the expected sales of new family homes in six months, as well as increase in traffic of prospective buyers. US housing starts meanwhile dropped 9% in June, to an 890,000 units annualized level, with some of the drop explained by heavy rains in the US South. US building permits also cooled off in June, to a 960,000 units annualized level from May's 990,000 units annualized level.

Canada – Inflation advanced in Canada to a 2.4% year on year rate in June, driven by higher food and energy prices. Core inflation, which excludes the effects of eight most volatile price series, mostly food and energy prices, also moved to a higher rate, 1.8% in June from May's 1.7%. Prices of clothes, autos and books have all contributed to the acceleration of the price increases in the month and seems to challenge the Bank of Canada's view that the recent spike in inflation is temporary and mostly attributed to increases in energy prices.

On the Canadian manufacturing front, May's manufacturing sales were up 1.6%, higher than the expected 1.0% increase and more than reversing April's 0.2% pull-back.

EU and US are increasing sanctions against Russia. Targets include Russian energy, defense and energy groups. The sanctions do not freeze Russian company's assets or limit their transactions but do prevent those firms from assessing US equity and debt liquidity for new financing for anything over 3 months. Energy companies and banks are highly dependent on USD funding. In addition, the EU is pledging to halt investment projects in Russia through the EIB, and possibly in the near future the EBRD.

Financial Conditions

US: US Federal Reserve policymakers remain determined to flatten the yield curve as much as possible, having indicated they expect 'exceptionally low levels of interest through 2014 with the Federal Reserve carefully calibrating the beginning of unwinding quantitative easing and undertaking that the Federal Reserve will keep rates low until mid 2015. The U.S. 2 year/10 year treasury spread is now 1.98% and the U.K.'s 2 year/10 year treasury spread is 1.74% - 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. It seems the top tier 6-9 investment banks will continue to command their market and possibly increase their share – as barriers to entry for newcomers have in our view been raised.

Influenced by the withdrawal of quantitative easing, the U.S. 30 year mortgage market rate has increased to 4.13% - (was 3.31%, end of November 2012 the lowest rate since the Federal Reserve began tracking rates in 1971), as the Federal Reserve effectively continues to give priority to incentivising home ownership. Existing U.S. housing inventory is at 5.2 months supply of existing houses. So the combined effects of low mortgage rates, near record high affordability, a more promising economic recovery, job creation, and low prices are finally supporting the housing market with housing inventory well off its peak of 9.4 months and we believe now in a more normal range of 4-7 months.

The VIX (volatility index) is 12.81 (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 currently offers 5 mutual funds:

- Portland Advantage Fund
- Portland Canadian Balanced Fund
- Portland Canadian Focused Fund
- Portland Global Banks Fund
- Portland Global Income Fund
- Portland Global Dividend Fund

Private/Alternative Products

Portland also currently offers 3 private/alternative products:

- Portland Focused Plus Fund LP
- Portland Private Income Fund
- Portland GEEREF LP

Market Commentary



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July 21, 2014

Net Asset Value:

At the close of business each day we publish the Net Asset Values (NAV) of our mutual funds onto our Portland website at <http://www.portlandic.com/prices/default.aspx>

Closed-End Fund

Spreads on the closed-end fund remain, in our view, very attractively priced to purchase.

The Portland Investment Counsel's 2013 Fourth Quarter Fund update is now available on the website.

At the close of business each day we publish the Net Asset Values (NAV) of our funds onto our Portland website at <http://www.portlandic.com/prices/default.aspx>

The price details published are replicated here below from which you can see we also highlight whether the funds share prices are trading at a premium or discount to their respective NAV.

Market Commentary



PORTLAND
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July 21, 2014

Source: Thomson Reuters, Bloomberg, Company reports

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