

# News Highlights

Owners. Operators. And Insightful Investors.

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**PORTLAND**  
INVESTMENT COUNSEL®

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

November 23, 2015

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## Energy Sector

**Royal Dutch Shell PLC** - we continue to believe Shell's announced transaction for BG Group plc, which should close in early 2016, makes strategic sense and re-positions the company down the cost curve. The NewCo will be a much less capital-intensive version of its former self with greater scale and scope around key focus areas and will allow the company to re-prioritise its investments and de-risk the dividend, in our view. We view Shell's deep-water portfolio as industry leading with a vast resource base to support it, its liquefied natural gas (LNG) positioning superior to its peers, which should put it in a relatively better position to improve margin capture and market share, and its downstream business as highly profitable. We were therefore pleased to learn that Shell announced last week the receipt of an 'unconditional' merger clearance from the **Australian Competition and Consumer Commission (ACCC)** leaving FIRB (Australia) and MOFCOM (China) as the last two remaining regulatory hurdles. As far as the update from the ACCC is concerned, we view it as positive as the 'clock' was not stopped again and the clearance was 'unconditional'. What we look for next in Australia is the update from FIRB - the decision maker here is the Commonwealth Treasurer. Next step in Australia is the approval from the FIRB. Here, the Treasurer must reach a view as to whether the deal is in the public interest or not. One of the factors the Treasurer takes into account is the effect on competition (and the Treasurer takes advice from the ACCC). Overall, this is a regulatory regime with less legal certainty and thus less predictable generally as the Treasurer has a broader degree of discretion. In most instances, things get approved, and we expect an update in weeks, not months. In China, MOFCOM (China) moved into Phase 3 on 5 November, which will last 'up' to 60 days. We expect 'manageable' remedies.

**US land rig count** fell 6 units week/week to 725, which is the thirteenth consecutive week of declines, led by decreases in horizontal oil (-7), vertical oil (-2), directional oil (-1), partially offset by gains in horizontal gas (+2), vertical gas (+1), and directional gas (+1). The US land rig count peaked 1 year ago at 1,864 rigs, a 61% decline year /year, which is a sharper decline compared to previous cycles 1 year from the peak (1997/98: 37%, 2001/02: 34%, 2008/09: 51%, 2011/12: 11%).

**US offshore rig count** dropped by 3 rigs to 30, which is still off June lows of 27 but down 43% year over year (YoY).

**Canadian rig count** was down 10 rigs and remains 62% off the level this time last year and is down 23% from its recent peak in July.

## Financial Sector

**Barclays PLC** bank announced it has reached a \$150 million settlement with the New York State Department of Financial Services (NY DFS) in respect of its investigation into Barclays' electronic trading of foreign exchange and FX electronic trading systems in the period 2009 to 2014. The civil penalty payable under the settlement will be reflected in Barclays' Q4 results. This follows a previous fine by NY DFS against Barclays in May, bringing the penalties imposed by the regulator against the bank for forex-related conduct to \$635 million.

**BNP Paribas SA** - Bloomberg reports that BNP Paribas (Suisse) will pay a penalty of \$59.8 million to receive a non-prosecution agreement from US Justice Department in probe of Swiss banks that helped Americans evade taxes, according to the Justice Department.

**Standard Chartered PLC bank's** Swiss unit will pay a \$6.3 million penalty as part of a deal it reached with the US Justice Department to avoid possible prosecution for helping Americans evade taxes, the department recently stated. The bank also agreed to cooperate in any criminal or civil proceedings involving US accounts and to adopt procedures for avoiding future misconduct, the Justice Department said. The Department, in return, will not prosecute the bank, provided that Standard Chartered fulfils follows the terms, the department said. (Source: Reuters).

**Standard Chartered** - Publishes prospectus for its previously announced rights issue. Expected timetable of principal events in UK includes: Record date for entitlements under the rights issue 17:00GMT November 18th, Start of offer period, shares trade ex-rights November 23rd, Publication of the results of the 2015 Bank of England stress tests ~December 1st, Rights Issue results announced by December 11th, Dealings in new shares 8:00 GMT December 11th.

**Wells Fargo and Company** named Tim Sloan, age 55, its president & COO. He will continue to report to CEO John Stumpf, age 62 (Wells Fargo has a mandatory retirement age of 65). Since 2014, Sloan has served as head of Wholesale Banking, a role he will retain. Reporting to him in his new roles are the heads of the company's other major business operations: Carrie Tolstedt (Community Banking); Avid Modjtabai (Consumer Lending); and David Carroll (Wealth and Investment Management). Prior to heading Wholesale Banking, Sloan, a 28-year veteran, served as Wells Fargo's chief financial officer from 2011 to 2014. In 2010, he was named chief administrative officer, overseeing the staff functions responsible for the company's brand, reputation management, stakeholder engagement and people development. These roles followed 23 years of experience in corporate, commercial and real estate banking, during which Sloan headed operations such as Commercial Banking, Commercial Real Estate and Specialized Financial Services.

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## Activist Influenced Companies

**Cable & Wireless Communications PLC** – John Malone-backed Liberty Global Plc offered to buy Cable & Wireless for £3.6 billion (\$5.5 billion) to extend its reach in the Caribbean. The stock offer for Cable & Wireless is valued at 78.04 pence per share, a premium of about 6% to Cable & Wireless's and roughly 40% from Cable & Wireless undisturbed price from before the October 21 discussions announcement. Shareholders will also receive a special dividend of 3 pence per share. Cable & Wireless offers home Internet, TV, landline and mobile phone, the so-called “quad play” package sought by companies such as Vodafone Plc and Liberty. Cable & Wireless had more than six million customers as of March, primarily in the Caribbean, Panama, Monaco and the Seychelles. The combined business would serve 10 million video, data, voice and mobile subscribers. Liberty Global has been growing through acquisitions. It bought Dutch cable operator Ziggo NV last year and British cable group Virgin Media in 2013. The Cable & Wireless deal comes nearly two months after Liberty Global and Vodafone ended talks regarding a swap of assets as they could not agree on valuations. Cable and Wireless said the Liberty Global offer values the company at about \$8.2 billion, including debt.

## Canadian Dividend Payers

Nothing new to report.

## Global Dividend Payers

**AusNet Services** – Victorian power grid owner AusNet Services is on track to meet its dividend guidance for the 2016 financial year after swinging back into the black in the first half as increased tariffs and energy volumes transmitted on its network boosted returns. AusNet, which is 51% owned by two cornerstone shareholders, Singapore Power and China's State Grid Corporation, reported net profit for the first half of 2016 of \$374.5 million, up from a loss of \$4.9 million in the same period a year earlier, when the bottom line was hit by a tax settlement and other provisions. Earnings before interest, tax, depreciation and amortisation (EBITDA) rose 22.9% to \$650.4 million on sales that climbed 10% to \$1.069 billion. An interim dividend of 4.265¢ was declared and AusNet said it was set to meet guidance for the full-year payout of 8.53¢ a share, up 2% on 2015. AusNet, which owns power transmission and distribution assets, and a gas distribution network, confirmed it would appoint an independent chairman by next year, after last month's announcement Singapore Power's designate Ng Kee Choe would step down.

**The Barry Callebaut Group**, the world's leading manufacturer of high-quality chocolate and cocoa products, signed a licensing agreement with the Naturex Group, the global leader in specialty plant-based natural ingredients.

**BHP Billiton plc** hosted a conference call to update the market on events at Samarco, following the fatal collapse of its tailings dam on November 5th. Our working assumption remains that the operation is out of action for at least 12 months and estimates for the clean-up cost range about \$0.5-1.0 billion (shared 50/50 with Vale ), which both companies are committed to providing. Samarco's US \$1.172 billion insurance is unlikely to provide sufficient cover for all civil damages liabilities, and full rehabilitation is likely to take several years. Ultimately it will be up to the government and communities to decide whether operations can restart. The estimated Net Present Value for the asset prior to the disaster was \$6.0 billion for 100% (\$3.0 billion for each company's share). BHP Billiton's market value has fallen \$12.7 billion since November 5th and if we strip out the mining sector movement since then its estimated BHP Billiton's market capitalisation has declined by \$2.7 billion and so the market appears to be broadly pricing in the assumption that Samarco is permanently shut down into BHP Billiton's valuation.

**Johnson Matthey plc** the world's biggest maker of metal catalysts for car emission-control devices, will pay £305 million to shareholders as a special dividend after selling two businesses. Reporting a dip in half-year profits, the company said it would make a special payout of 150 pence a share, on top of a regular interim dividend increased 5% to 19.5p. The company had said in July it might return cash to shareholders after making £380 million from the sale of its Gold and Silver Refining and Research Chemicals businesses, provided it did not make any major acquisitions. The company, which also refines and recycles platinum group metals, posted a 4% fall in underlying pretax profit to £208.3 million for the half year through September, as a poor performance in its precious metal products business due to low prices offset strong growth in emission control technologies. Platinum prices hit their lowest in nearly seven years this week. Johnson Matthey said as a result of challenging conditions in several key markets, it had started a restructuring review particularly in its Process Technology division, which sells catalysts and technologies to the oil and petrochemical sector. It said the restructuring was expected to cut costs by around £30 million annually and had an associated one-off charge of around £40 million. Johnson Matthey Chief Executive Robert MacLeod said that the cost-cutting program should enable the company to return to growth next year. Automobile emissions-control system makers are also expected to gain from the Volkswagen emissions-cheating scandal, seen likely to lead to tighter regulation to make cars more environmentally friendly.

**Wal-Mart, Inc.** reported 3rd Quarter 2016 Earnings per Share (excluding lease adjustments of \$0.04) of \$0.99, \$0.01 ahead of consensus. Walmart US comps grew 1.5%, in line with our estimate. Operating margin fell 0.53%, driven by a 1.03% increase in Sales and Administration costs as a percentage of sales, partially offset by a 0.59% increase in gross margin.

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## Economic Conditions

**US industrial production** fell unexpectedly in October. The 0.2% drop (+0.3% YoY) was the second setback in a row, with utilities and mining weighing on the headline. (No revision to September, but the 0.1% decline in August is now showing a 0.1% gain.) These two components, account for about 23% of the total. Utilities (11% weight) took a 2.5% hit....remember it was the warmest October in decades. Mining (12% weight) also declined again, down 1.5% in the month or 6.9% below a year ago, the steepest year/year drop in 6½-years. Conversely, manufacturing (100-11-12=77% weight) output rose 0.4%, the first improvement since July. (Note that hours worked in the sector rose for the first time in three months.) All of the support was provided by motor vehicles and parts.....+0.7%.

**Greece** - Greece and its international creditors said on Tuesday they reached an agreement on the country's next round of economic changes a deal that is meant to unlock as much as €2 billion (\$12.77 billion) in loan money.



## Financial Conditions

US Federal Reserve policymakers remain determined to signal that although Quantitative Easing has stopped, the stimulus remains via keeping rates at present low until earliest December 2015. The US 2 year/10 year treasury spread is now 1.35% and the UK's 2 year/10 year treasury spread is 1.27% - 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 US 30 year mortgage market rate has increased to 3.97% (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 US housing inventory is at 5.0 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 15.47 (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.

**And Finally:** according to the OneShift 2014 job seeker survey, the 10 most bizarre questions asked by Australian employers are as follows: 1) Bring an item with you to the interview that best suits your personality. 2) Imagine a pen that could do anything. How would you sell it to me? 3) On a day-to-day basis, what number do you think of the most? 4) If you could have a day on earth where you could do one thing as much as you wanted what would it be? 5) If you started dating another employee, would you inform the manager about your relationship? 6) What would you expect to see written on your gravestone? 7) Name the seven dwarves from Disney's Snow White. 8) How would you move three chairs from one end of the room to the other? 9) Here's a pen between us. How would you get the pen over to me? 10) Would you wear a sombrero at the airport so company guests can identify you during pick-up?

## 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 Private Income Fund
- Portland Global Energy Efficiency and Renewable Energy Fund LP
- Portland Advantage Plus Funds
- Portland Private Growth Fund

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PIC15-058-E(11/15)