

News Highlights

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PORTLAND
INVESTMENT COUNSEL®

Established in 2007

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

December 11, 2017

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Owner Operated Companies

Brookfield Asset Management Inc. has agreed to acquire Lampe Equity Management GmbH, an asset manager of the CEE Group, Inc. from Bankhaus Lampe KG, a private bank that provides banking products and services. Both Lampe Equity Management and Bankhaus Lampe are based in Germany. CEE Group is a provider of civil, structural engineering and MEP design services, while Lampe Equity Management is a subsidiary of Bankhaus Lampe. Lampe Equity Management has around €1.3 billion (USD1.53 billion) worth assets under management. Upon completion, CEE Group will continue to operate under the CEE brand. As part of the transaction, around 40 employees of Lampe Equity Management at the Hamburg location will join Brookfield. Detlef Schreiber is the chief executive officer of Lampe Equity Management and CEE Group. Following the transaction, Bankhaus Lampe will remain investor in Lampe Equity Management. The transaction is expected to close by end of 2017.

Walgreens Boots Alliance, Inc. said it would buy a 40% stake in Chinese pharmacy chain operator Sinopharm Holding GuoDa Drug Store Co., Ltd. (GuoDa) as the U.S. drugstore chain seeks to expand in the country's fast-growing healthcare market. Walgreens said it would buy the minority stake from China National Accord Medicines Corp. Ltd. for about \$416 million. The deal comes when the Chinese government has been encouraging private investments and equity from abroad in its healthcare industry. Healthcare expenditure in China is expected to reach \$1.1 trillion by 2020, according to an estimate by the U.S. Department of Commerce. GuoDa, which operates and franchises 3,500 retail pharmacies across 70 cities in China, said the Walgreens investment would help its nationwide expansion plans.

Energy Sector

U.S. land rig count increased by 1 rig week/week to 909, which is the fifth consecutive week of gains. The rig count was driven by increases in Horizontal Oil (+5) and Directional Gas (+1), offset by declines in Directional Oil (-3) and Vertical Gas (-2), as Vertical Oil and Horizontal Gas remained flat week/week.

Canada rigs down 3 rigs week/week.

International rigs averaged 942 in November, with land rigs up 12 and offshore rigs down 21 month/month, led by declines in Middle East (-1 land, -6 offshore) and Europe (-2 land, -4 offshore), partially offset by gains in Latin America (+6 land, -2 offshore), while Africa (+3 land, -3 offshore) and Asia Pacific (+6 land, -6 offshore) remained flat month/month.

Baytex Energy Corp. announced that its Board of Directors has approved a 2018 capital budget of \$325 to \$375 million, which is designed to generate average annual production of 68,000 to 72,000 boed. As for 2017, Baytex is targeting 2018 capital expenditures to approximate funds from operations in order to minimize additional bank borrowings. The capital program is expected to generate internal rates of return in excess of 50% on a per well basis, which reflects efficiencies on an annual basis of approximately \$12,000 per boed (\$14,000 per boed including facilities). The company's 2018 capital budget assumes a WTI (West Texas Intermediate) price of US\$55/bbl. The 2018 program is approximately 60% weighted to the first half of the year. Based on the mid-point of Baytex's guidance range of 70,000 boed, approximately 51% of its production is expected to be generated in the Eagle Ford with the remaining 49% from Canada. Baytex has an ongoing board renewal process led by the Nominating and Governance Committee of the Board. Since 2013, Baytex has added three independent Board members from various professional backgrounds. As part of this renewal process, John Brussa and Rusty Goepel, two long-standing board members will be retiring at the 2018 Annual Meeting of Shareholders to be held in May 2018.

Financial Sector

Bank of Montreal (BMO) posted a Q4 profit of \$1.23 billion vs \$1.34 billion year/year, with a \$112 million charge related to hurricane impacts on the insurance business, and higher credit loss provisions driving a large part of this year/year decline. While both the Canadian and U.S. Personal and Commercial Banking (P&C) segments posted stronger results, the Wealth Management (insurance impacts) and BMO Capital Markets (lower revenues, higher expenses and credit losses) both posted softer results year/year. The CET 1 ratio was 11.4%, up from the 10.1% level year/year. Credit losses were higher at \$208 million vs \$174 million year/year, with an increase in provisions in several segments. While results were modestly softer than expectations, the asset, capital, and credit protection for the bank remain strong in our view. BMO increased its quarterly dividend by \$0.03 to \$0.93, up 3% (vs. consensus of 2%).

Barclays PLC sold a 7% stake in Johannesburg-based Barclays Africa Group Limited on December 5, the latest and likely last in a series of such sales as it ends more than 90 years as a major presence on the continent. Barclays said after the sale its stake in the African division would be 14.9%, which represents its desired long-term goal and no further sales are planned. The British bank first announced in March 2016 that it would sell most of its then 62% stake in Barclays Africa over two to three years, as the bank

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refocused its strategy on the U.S. and Britain under Chief Executive Jes Staley. (Source: Reuters)

Activist Influenced Companies

Nothing significant to report.

Dividend Payers

Aryzta AG is said to have sold La Rousse Foods Ltd. for roughly €30 million. There were some rumors last September about such a deal. Aryzta acquired La Rousse in 2015 for €27 million. The company had sales of €45 million. Picard Surgelés announced that it intends to refinance the total of its existing bonds. Management is currently road showing in Europe. The gross proceeds will be used to fund distributions to the shareholders, among others. The plan is to pay out a dividend of €110 million (Aryzta has a 49% stake). Generous dividend for a company with a net debt to EBITDA of 7x as of September 30th (Moody's). Picard closes its financial year as at the end of March, so that Aryzta will see an inflow of more than €50 million in Q4 2018 (Aryzta closing as of July 31st). Both news go in the right direction for Aryzta, with an estimated, nonoperational cash inflow of €80 million. As a reminder, Aryzta had a net debt of €1.7 billion at the end of July 2017. Management is targeting €1 billion free cash flow in the coming four years, including disposal proceeds and Picard dividend.

Nestlé SA – the world's largest food group is spending \$2.3 billion to buy Atrium Innovations Inc., a Canadian nutritional products company, from private equity group Permira as it seeks to build its portfolio of consumer healthcare businesses.

Pattern Energy Group Inc. announced its Meikle Wind power facility received the Project Excellence Award from Clean Energy BC. The 179 megawatt (MW) Meikle Wind facility is located near Tumbler Ridge in British Columbia. "Pattern Energy's Meikle Wind facility is an outstanding example of how to bring together zero-carbon energy generation, local economic development and sustainable business. We are honored to have this project in British Columbia and we look forward to many more," said Jae Mather, Executive Director of Clean Energy BC. The 179 MW Meikle Wind facility consists of 61 GE wind turbines, including 35 3.2 MW turbines and 26 2.75 MW turbines. The facility's innovative layout, developed in collaboration with GE, incorporates two different turbine models consisting of varying rotor sizes and hub heights. This design was developed to capture the most energy from the ridgelines, accounting for varying wind speeds, wind shear, turbulence and inflow angles. Meikle Wind is generating strong benefits for the province with an estimated \$70 million in payments for property taxes, Crown lease payments, wind participation rent, and community benefits over the first 25 years of operations. The facility commenced commercial operations in the

first quarter of 2017 and operates under a 25-year power purchase agreement with BC Hydro.

Roche Holding AG last week released more detailed data about the phase 3 IMpower 150 study. The study showed that people treated with Tecentriq + Avastin + chemo had a 38% reduced risk of their disease worsening or death (progression-free survival, PFS) compared with those who received Avastin + chemo. The benefit of PFS after one year with Tecentriq doubles the 12-month landmark PFS with the combination of Tecentriq and Avastin + chemo showing a 37% PFS rate compared to 18% with Avastin + chemotherapy only. IMpower 150 is the first positive phase 3 combination trial that showed a cancer immunotherapy reduced the risk of the disease getting worse when used as a 1L treatment in patients with interleukin-1 non-small cell lung cancer (1L NSCLC). We find this data impressive. Roche had already announced that the overall survival curves look encouraging with final read-out expected in 1st Half 2018. **Also today Roche announced a second positive phase III study of Tecentriq: Phase 3 IMmotion 151 met its co-primary endpoint by demonstrating that the combination treatment Tecentriq + Avastin reduced the risk of disease worsening or death (PFS) in a statistically significant and clinically meaningful fashion in patients with previously untreated metastatic renal cell carcinoma (RCC) versus standard-of-care treatment with sunitinib. IMmotion 151 data will be presented at an upcoming oncology conference in 2018. Roche plans to discuss this data with health authorities globally. Top-line results from the co-primary endpoint of overall survival (OS) are not yet mature.**



Economic Conditions

Canada housing starts in Canada jumped to 252,200 units annualized in the month of November, from 222,800 units annualized in October and against the expectations for a pull-back to a 215,000 units annualized read. The starts growth was driven by the multi-units segment, in particular in Ontario.

Building permits, meanwhile, decelerated modestly in October, up 3.5% compared to September's 3.8% advance, but ended up way ahead of the expectations, which were counting for a 1.5% improvement.

Canadian goods and services trade balance resulted in a lower deficit for the month of October, at \$1.47 billion, compared to September's \$3.18 billion deficit. Exports advanced 2.7% in the month, led by chemicals and agriculture, while imports decreased by 1.6% in the month, dragged lower by imports of road vehicles.

U.S. Nonfarm payrolls rose a better-than-expected 228,000 in November, well above the past year mean (173,000), while gains the prior two months were marked up slightly. Nearly every industry shared in the bounty (apart from information), with manufacturing and construction extending a four-month hiring streak. The

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employment rate slipped to 60.1% of the adult population, but it's still nearly 2 ppts above the cycle nadir. The jobless rate held at a 17-year low of 4.1%. While the "all-in" U6 jobless rate rose slightly, this was a mild payback from October's four-tenths tumble. The duration of joblessness continued to shorten. Once again, wages surprised on the low side. Average hourly earnings increased 0.2% after a rare decline the prior month. This lifted the yearly rate to 2.5%, well within the range of the past year and nowhere near strong enough to spark inflation. This follows news that unit labour costs continued to trend downwards in Q3, a rare development this late in an expansion—which partly speaks to automation anxiety spreading to more industries.

U.K. and European Union: U.K. Prime Minister, Theresa May and EU announced that a deal has been reached to move the Brexit talks into the next stage. The meatier Phase 2 negotiations are set to begin next week, on what exactly a post-Brexit future would look like trade-wise, etc. And so still a longway to go here beyond merely agreeing on divorce payments (of about £50 billion) or what an Irish border might look like.

U.K. Report on Jobs, a survey of recruitment consultants, for November is mixed with positive trends in job placements in the month but a slight reduction in the rate of growth in demand for staff. The data indicates permanent placements rose at the quickest pace for three months and growth of temporary billings rose slightly after softening in October. However, while demand for staff and pay growth remains high, in both cases the rate of growth slowed in November. Demand for staff remains much stronger in the private sector than the public sector. Looking into 2018, the report argues the government needs to agree transitional arrangements for freedom of movement of EU workers and define the access U.K. employers will have to EU workers after Brexit.

Financial Conditions

Bank of Canada (BoC): held interest rates unchanged last week, Governor Poloz again surprised markets in our view with a less upbeat analysis on the markets. The BoC remained "cautious" on interest rates which sounds like a message towards pushing out their next rate rise from January to March/April. The paragraph in the BoC statement yesterday that caught analysts attention was this one: "Inflation has been slightly higher than anticipated and will continue to be boosted in the short term by temporary factors, particularly gasoline prices. Measures of core inflation have edged up in recent months, reflecting the continued absorption of economic slack. Revisions to past quarterly national accounts have resulted in a higher level of GDP. However, this is unlikely to have significant implications for the output gap because the revisions also imply a higher level of potential output. Meanwhile, despite rising employment and participation rates, other indicators point to ongoing – albeit diminishing – slack in the labour market." The issues which we believe arise from the statement are: (i) Inflation: what transitory

factors besides gasoline is Mr. Poloz talking about (and does the Bank know gas prices are coming down)? (ii) Potential output: do the revisions point to a higher potential output? (iii) Labour market slack: what are the "other indicators" that they reference that point to ongoing slack? Generally, we share the sentiment of other analysts that he statement felt more like the BoC was picking certain indicators to justify the cautiousness rather than being cautious because of the overall data.

The U.S. 2 year/10 year treasury spread is now .57% and the U.K.'s 2 year/10 year treasury spread is .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 costs of capital.

Influenced by the withdrawal of quantitative easing, the U.S. 30 year mortgage market rate has increased to 3.94% (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 9.89 (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 augurs well for quality equities.

Mutual Funds

Portland Investment Counsel Inc. currently offers 8 Mutual Funds:

- [Portland Advantage Fund](#)

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- [Portland Canadian Focused Fund](#)
- [Portland Global Income Fund](#)
- [Portland Global Banks Fund](#)
- [Portland Global Dividend Fund](#)
- [Portland Value Fund](#)
- [Portland 15 of 15 Fund](#)

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- [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](#)
- [Bay & Scollard Development Trust](#)

Individual Discretionary Managed Account Models - [SMA](#)

Net Asset Value:

The Net Asset Values (NAV) of our investment funds are published on our Portland website at <http://www.portlandic.com/prices/default.aspx>

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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, 'ROE' return on equity, 'ROTE' return on common equity.

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