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. August 14, 2018

Owner Operated Companies

Brookfield Asset Management Inc. – earned USD $1,664 million on revenue of USD $13,276 million in the second quarter of 2018. This compares with earnings of USD $958-million on revenue of USD $9,444 million in Q2 of 2017. Bruce Flatt, Chief Executive Officer of Brookfield, stated: "We continue to see strong interest from institutional investors in our real assets strategies, as evidenced by the closing of $11 billion of capital to date for our most recent flagship real estate fund. We ended the quarter with record liquidity of $33 billion, and we continue to find attractive opportunities to invest this capital including the recent privatization of GGP Inc., the acquisition of a major gas gathering infrastructure system, and the successful acquisition of Westinghouse Electric [Company LLC.]" Net income reached USD $1.7 billion in the quarter and USD $6.6 billion for the last 12 months, both significant increases over the comparable periods. The increase in the quarter reflects contributions from recent acquisitions across each of the company's businesses, transaction gains and strengthening valuations for a number of the company's assets. Second quarter funds from operations (FFO) were USD $790 million, including USD $132 million of disposition gains. Excluding disposition gains, second quarter FFO was USD $658 million, 17% higher than the comparable period. Fee-related earnings continue to increase as a result of the growth in fee-bearing capital from the company's private funds and higher performance fee income from Brookfield Business Partners L.P. FFO from invested capital increased 26% over the comparable period reflecting contributions from recent acquisitions, additional home sales in the company's North American residential business, and improved performance by businesses owned within the company's private equity operations. Disposition gains included the sale of a 13% interest in the company's graphite electrode manufacturing operations and the sale of the company's interest in a real estate brokerage business.

Linamar Corporation - earned $197.1 million on revenues of $2.15 billion in the second quarter of 2018. The company earned $161.9 million on revenues of $1.76 billion in the same period last year. Sales increased 22.1% over the second quarter of 2017 to reach $2.2 billion (a new record). Operating earnings increased 26.3% over Q2 2017 to reach $272.3 million (a new record). Net earnings were up by 21.7% and earnings per share, on a diluted basis, were up 21.6% over Q2 2017 ($197.1 million and $2.98, respectively, both record levels as well). Continued business wins maintain strong launch book at nearly $4.5 billion. Industrial segment sales were up 80.2% and operating earnings were up 146.8% thanks to the acquisition of MacDon Industries Ltd., market share gains and strong volumes for access equipment at Skyjack Inc. Industrial segment represents nearly 50% of overall earnings thanks to solid growth. Transportation segment sales were up 7.2% thanks to launches despite key customer production cuts. "We are thrilled to announce another quarter of record sales and earnings, both growing at a strong double-digit level," said Linda Hasenfratz, Linamar's Chief Executive Officer. "Our diversification strategy is paying off in spades, with our industrial segment now rivalling transportation in terms of earnings thanks to robust performance at both MacDon and Skyjack. Launches are doing a fantastic job of growing content per vehicle and sales, both key to long-term growth, and quoting activity remains at a very high level. Our future has never looked brighter despite political uncertainty."

Energy Sector

Nothing significant to report.

Financial Sector

Nothing significant to report.

Activist Influenced Companies

Barclays PLC - Edward Bramson's activist investment fund has stepped up the pressure on Barclays by saying it is engaging with the bank on its search for and the mandate of a chairman to replace John McFarlane. Giving details of his approach to Barclays for the first time, Mr. Bramson's Guernsey-based Sherborne investment vehicle also said in a public filing that it was discussing capital, earnings and costs with the bank in which it owns a 5.4% interest. Barclays said in April that it had started the process of searching for a successor to Mr. McFarlane, who joined the bank in 2015 with a promise to stay in the role for at least four years. He has long been expected to retire in 2019, but Mr. McFarlane told shareholders at the annual meeting in May that he would leave only "when the time is right", adding that "while some might wish so, you are not getting rid of me yet". (Source: Financial Times)

Nomad Foods Limited reported financial results for the three and six month periods ended June 30, 2018, which included a reported revenue increase of 6.6% to €488 million. Organic revenue growth was 1.3%, while reported profit for the period was €31 million. Adjusted EBITDA increased 12% to €89 million. Reported EPS was €0.18, while adjusted EPS increased 22% to €0.28. The company raised its 2018 guidance to €365 to €370 million of adjusted

EBITDA and €1.14 to €1.17 adjusted EPS. Stéfan Descheemaeker, Nomad Foods' Chief Executive Officer, stated, "We reported solid second quarter results, highlighted by 1.3% organic revenue growth, 90 basis points of Adjusted EBITDA margin expansion and 22% Adjusted EPS growth. Performance was particularly encouraging given this year's earlier Easter timing and the highly publicized summer heat waves throughout Europe. Recent acquisitions are proving complementary. Goodfella's is performing well in our first few months of ownership and Aunt Bessie's [Limited], which closed on July 2nd, is expected to be immediately accretive. We are pleased with our year-to-date progress and are on pace to deliver another year of top and bottom line growth." Noam Gottesman, Nomad Foods' Co-Chairman and Founder, commented, "Second quarter results demonstrate the strength of our business model and the execution ability of our management team. We remain uniquely positioned to capitalize on the favorable macro trends occurring within the frozen food space and are excited by the potential of our portfolio in both the near and long-term."

Dividend Payers

Aryzta AG - Capital increase of €800 million through rights issue which we believe should provide enough leeway to strengthen the balance sheet, implement the strategy, and pay for the restructuring. Aryzta has been compliant with all covenants in fiscal year 2018. More details to be announced on October 1. Q4 trading was in line and thus fiscal year EBITDA guidance of €296-€304 million was met, which comes as a slight relief after a series of profit warnings. Aryzta is now targeting cost savings of €90 million per annum by 2021, thereby incurring restructuring costs of €150 million over the next three years. Deleveraging plan confirmed: As previously communicated, comprising of greater than or equal to €450 million from asset disposals and the balance from cash flow generation.

GEA Group AG - According to Bloomberg (July 31), investor Groupe Bruxelles Lambert increased its stake in GEA to 7.29% from 5.49% earlier.

RioCan Real Estate Investment Trust, in our view, continues to execute well on its dual strategy of divesting non-core properties in secondary markets while investing in its development program, which is largely residential. At the same time, fundamentals for well-located retail properties remain strong and the Real Estate Investment Trust (REIT) reported solid results for the quarter. In our view, this provides further evidence that, while sentiment towards retail properties remains negative, the story on the ground is positive. For Q2 2018, RioCan reported FFO per diluted unit of $0.46. FFO per unit was up 2.5% from the year-ago quarter and ahead of consensus of $0.44. The growth was largely from internal growth and increased value from marketable securities and was offset by dilution from asset sales and increased general and administrative from severance costs. Same-property Net Operating Income was up 2.1%, and even stronger (2.5%) in urban markets. On an annualized basis, RioCan now generates 81% of its revenue from Canada's six largest markets, with a particular focus on the GTA (44%). As this number grows, we expect internal growth to trend higher. Of the $2.0 billion of assets targeted for sale, RioCan had completed or agreed to sell $876 million of properties at a weighted average cap rate of 6.34%, up $293 million from Q1 2018. Additionally, the REIT has conditional agreements to sell fourteen properties for a total of $279 million. Should all of these asset sales close, the REIT will have sold 60 properties for $1.15 billion of its $2.0 billion target. With RioCan's units trading at a discount to NAV, repurchasing units is accretive, and helps to mitigate dilution. During the quarter, the REIT repurchased and cancelled 5.3 million units for $126.2 million, bringing the total repurchased over the past 12 months to 15.1 million for a total cost of $366.1 million. With an additional $800 million of properties targeted for sale, we expect this pace of buybacks to continue over the next year.

Economic Conditions

The Financial Post reported that news of Canada's apparent ejection from the list of countries that stand to benefit from Saudi Crown Prince Mohammed Bin Salman's largesse, echoed comments made by Stephen Poloz, the Bank of Canada governor, last month. In an interview with the Financial Post, Mr. Poloz shared his thoughts on whether Canadian aluminum and steel exports might push through U.S. duties the same way lumber shipments had. Mr. Poloz highlighted that the issue was bigger than that. "It could be that we're putting too much energy into it," he said, referring to the tit-for-tat response to the Trump administration's tax on metal imports. "But at the same time," Poloz continued, "if we're not going to spend energy on it, just because this is small, or that's not going to have much effect, what good are we? There are principles involved." Principles now are driving relations between Canada and a country that had excellent potential to help Prime Minister Justin Trudeau with his quest to make Canadian companies less reliant on the United States. Late last week, Freeland, and then her department, tweeted statements of disappointment over the imprisonment of advocates for women's rights by Saudi authorities. There was no reason to pay any attention to those tweets. Canada has little, if any, influence in the Middle East, and those are the sorts of comments democratic countries direct at their less-democratic trading partners all the time. Except countries such as Saudi Arabia are becoming more sensitive to scolding from abroad. The kingdom responded to Freeland's tweet in shocking fashion, expelling the Canadian ambassador and freezing "all new business" with Canada. All this should be a reminder that politics now represent one of the biggest threats to the global economy.

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U.S. total Consumer Price Index (CPI) increased 0.2% in July, keeping the annual change at 2.9% year/year, which still matches the fastest pace in more than 6½ years. Energy prices slipped 0.5% (lower gasoline, electricity and natural gas prices) while food prices inched up 0.1% (about the average pace over the past year owing to intense retail competition). The core CPI also increased 0.2%, but it nudged the annual change up a tenth to 2.4% year/year. This is now the fastest core inflation rate in almost a decade (it was 2.5% in September 2008). For the core, the 3-month trend has turned up again – its prior slippage was becoming a concern – it's now 2.3% annualized, up from 1.7% last month and 1.8% three months ago. Among the major components, nothing stood out too much, which suggests the core pressure was broad based. Core goods inched up 0.1%, but importantly the annual change is now zero, the first non-negative print in almost 2½ years. Core services increased 0.3% keeping the annual change at 3.1% year/year, which still matches the fastest pace in almost two years. Labour costs are an important driver here.

The U.K. Report on Jobs, a survey of recruitment consultants, for July indicates a continuation of recent trends, with demand for staff remaining robust and pay pressures at historically high levels, despite growth slowing over the month. Growth in permanent placements remains high but was the least marked since October last year. The rate of growth in temporary billings, recovered from June's low and is back above historical average levels. At the same time, there continues to be a reduction in the availability of permanent staff which continues to drive wage inflation. Starting salary inflation for permanent jobs slowed slightly in the month but remains above the long-run average, driven by continued candidate shortage. Growth in pay for temporary staff accelerated in July and was only slightly below April's two year peak. The report's Vacancy Index, a measure of demand for staff, saw continued growth in July, above the long-run trend and the highest since November last year, with demand continuing to be higher in the private sector than the public sector.

Financial Conditions

China's central bank (PBoC) on Friday (August 10) released its Q2 2018 Monetary Policy report, which reiterated its neutral and prudent stance despite cutting reserve requirement ratio (RRR) three times so far this year (in January, April, and July, respectively). Against a backdrop of trade tensions, geopolitical shifts, and policy normalization by major central banks, PBoC says it will strike a balance of the three key tasks of stabilizing economic growth, pushing structural adjustments, and preventing risks, vowing to fend off systemic financial risks. The central bank will make policies more forward-looking, flexible and effective, maintain proper control over the "floodgate" of money supply while still keeping liquidity at a reasonable level, according to the Q2 2018 monetary policy report.

The U.S. 2 year/10 year treasury spread is now 0.25% and the U.K.'s 2 year/10 year treasury spread is 0.55% - 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 two-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 4.59% (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 4.0 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 13.77 (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.

And finally.... Turkey President Erdogan failed to smooth markets over the weekend and said that the U.S. is seeking to "stab it in the back" after the U.S. imposed sanctions last week when Turkey failed to extradite a U.S. Preacher imprisoned in the country. The Trump administration doubled tariffs on Turkish steel and aluminum after Turkey refused to free an American pastor who has been in detention for nearly two years. The Turkish stock markets have fallen 17% and government borrowing costs have soared to 18% with inflation hitting 15%. Markets are calming a little today with Erdogan doubling down again against the markets (i.e. he will die before raising interest rates), I wonder if this is how George Soros felt in 1992 when the Bank of England purchases allowed Soros enough time to build up $1.5 billion position against the British Pound and made $1 billion.

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
- Portland Advantage Plus - Everest and McKinley Funds
- 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) 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, 'ROE' return on equity, 'ROTE' return on common equity.

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