News Highlights

Owners. Operators. And Insightful Investors.

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Established in 2007

PORTLAND INVESTMENT COUNSEL®

Our views on economic and other events and their expected impact on investments. November 12, 2018

Owner Operated Companies

Brookfield Asset Management Inc. earned USD $941 million on revenue of USD $14,858 million in the third quarter of 2018. This compares with earnings of USD $992 million on revenue of USD $12,276 million in Q3 of 2017. Bruce Flatt, Chief Executive Officer of Brookfield, stated: "We had another strong quarter. We ended the quarter with liquidity of $32 billion, which we expect to deploy into opportunities across our listed and private funds. Fundraising continues to be strong, including $18.5 billion of capital to date into two of our most recent flagship funds." Net income was $6.5 billion for the last 12 months and $941 million in the quarter. The increase in the last 12 months reflects contributions from recent acquisitions across each of the company's businesses, a higher level of appraisal gains and transaction gains. Third quarter funds from operations (FFO) were $1.1 billion. Fee-related earnings increased to $320 million, a 72% increase over the prior period. The board declared a quarterly dividend of $0.15 per share (representing $0.60 per annum).

Carnival Corporation launched cruise joint venture in China. The world's largest leisure travel company and China State Shipbuilding Corporation set to formally launch cruise joint venture this week under the name CSSC Carnival Cruise Shipping Limited. The new cruise company in China will purchase two existing ships from Costa Group, with the first ship expected by end of 2019 to begin serving guests as part of the JV fleet. The joint venture also finalized previously announced agreement for world's first two new cruise ships to be built in China for the Chinese cruise market, the first of which will be delivered in 2023. As the world's top outbound tourism market, China's 142 million outbound travellers spent an estimated $258 billion traveling abroad in 2017, according to the United Nations World Tourism Organization (UNWTO). By comparison, the Chinese cruise industry served only about 2.5 million cruise passengers last year, representing less than 2% of China's outbound global travellers. As a large, embryonic and underpenetrated cruise market with continued long-term projections for outbound tourism growth, China represents a significant opportunity for the cruise industry to raise awareness, consideration and demand for cruise vacations in coming years. As the industry continues to grow and develop in the region, China is widely expected to eventually become the largest cruise market in the world.

The Kraft Heinz Company has agreed to sell its Canadian natural cheese business to Parmalat S.p.A in a CAD $1.62 billion ($1.23 billion) deal that will help Kraft trim its debt and extend the North American footprint of Parmalat owner Lactalis. The deal comes a month after the new United States-Mexico-Canada Agreement (USMCA) was signed, under which Canada partially opened its protected domestic market to the United States. The cheese business being sold by Kraft, which includes brands like Cracker Barrel, P'tit Quebec and aMOOza, generated about CAD $560 million in net sales in 2017. Under the deal, expected to close in the first half of 2019, Kraft will sell its production facility in Ingleside, Ontario and transfer 400 employees to Parmalat. The U.S. food group will continue to own and market other cheese products, including Philadelphia, Cheez Whiz and Kraft Singles, which are processed in Quebec.

Linamar Corporation earned $113.2 million on sales of $1.83 billion in the third quarter ended September 30, 2018. This compares with a profit of $107.3 million on sales of $1.54 billion in the same quarter a year earlier. Sales increased 18.6% over the third quarter of 2017 ("Q3 2017") to reach $1.8 billion, while operating earnings increased 13.7% over Q3 2017 to reach $161.4 million. Net earnings were up 5.5% and EPS, on a diluted basis, up 5.6% over Q3 2017 reaching $113.2 million and $1.71 respectively. FCF continued to bring net debt levels down. Business wins tracking significantly over prior year period, strengthening launch book to over $4.5 billion. Industrial segment sales up 86.2% and operating earnings up 121.3% thanks to the acquisition of MacDon Industries Ltd., market share gains and strong volumes for access equipment at Skyjack Inc.

Energy Sector

Northland Power Inc. reported Q3 2018 EBITDA (adjusted) of $196.8 million compared to consensus of $204.5 million ($176.4 million - $216.0 million). FFO came in at $63.9 million reflecting a payout ratio of 83.1%. Northland has lowered guidance for 2018 adjusted EBITDA to be in the range of $870 to $900 million (formerly, $860 to $930 million) and 2018 FCF per share to be in the range of $1.75 to $1.95 (formerly, $1.70 to $2.00). The adjustment reflects year-to-date results including unusually lower than historical average offshore wind speeds in northern Europe for the first nine months of the year.

Financial Sector

Canada's Banks Doing Fewer Deals as global investment banks win more Canadian Mergers & Acquisitions (M&A) business: Over the weekend, the Globe and Mail highlighted that, with Canada's banks closing the books on the fiscal year at the end of October, the value of stock sales are down from a robust 2017, while independent dealers also appeared to grab a bigger share of the market. According to the article, data from Thomson Reuters indicates that domestic equity offerings fell by 28% in the year that ended October 31, to $32.2 billion from $44.6 billion in the same period a year earlier. For the Canadian banks, the article notes that the 'Big 6' largely missed out on raising money for cannabis companies, as bank-owned firms only recently started to do business with marijuana producers, primarily because of concerns with U.S. regulations. In contrast, the previous year featured large equity offerings from utilities and energy companies, clients with strong ties to the big banks. Amongst the league tables, The Toronto-Dominion Bank (TD) was the top domestic equity underwriter with $4.4 billion of stock sales, but was down from $7.7 billion a year ago. Royal Bank of Canada ranked second, with equity sales of $2.8 billion, down from $9.7 billion the previous year. Canaccord Genuity LLC, the largest independent investment dealer, saw its value of deals double over the past 12 months to $2.3 billion, and ranked ahead of The Bank of Nova Scotia and National Bank of Canada. On the M&A front, while the value of deals involving Canadian companies climbed by 28% versus a year ago to US$272 billion, many of the biggest takeovers were done outside of Canada. As such, global investment banks occupy the top three slots in Canadian M&A activity.

Fewer Canadian independent asset managers: – Over the weekend, following a wave of transactions involving Canadian money managers, Bloomberg reported that closely held asset manager Mawer Investment Management has hired Scotiabank to explore options such as a sale. In an email statement to Bloomberg, Mawer's president Michael Mezei indicated that "given recent activity in the industry, Mawer has engaged an adviser to obtain more information on the options available to the firm, as part of our strategic planning process." Further, Mr. Mezei noted that "no decision has been made to change firm ownership. Our focus remains on delivering excellent long-term investment results for our clients." The article notes that Canada's big banks have been the most active buyers of wealth management industries, with TD completing the CAD $792 million purchase of Greystone Capital Management, Inc., and Scotiabank acquiring MD Financial Holdings Inc. (CAD $2.6 billion) and Jarislowsky, Fraser Limited (CAD $950 million). Founded in 1974, Mawer oversees more than CAD $50 billion for individual and institutional investors across all major asset classes.

European financial regulators are discussing whether to supervise big technology companies more closely in response to recent moves into financial services by groups such as Amazon.com Inc. and Google (Alphabet Inc.), according to one of Europe's most senior central bankers. Olli Rehn, governor of Finland's central bank and a member of the European Central Bank's governing council, said the issue of big tech's encroachment into the financial sector had prompted "a very lively discussion by financial supervisors and central banks in Europe". His comments on Sunday at the Financial Times Middle East Banking Forum in Dubai will be welcomed by many senior bankers who have been complaining about the uneven playing field as they worry about competing head-on with big tech groups. (Source: Financial Times)

Activist Influenced Companies

Liberty Latin America Ltd. (LLA) announced its financial and operating results for the three months and nine months ended September 30, 2018. CEO Balan Nair commented, "In Q3, we returned to rebased revenue growth driven by our high-speed broadband strategy across LLA and strong growth in Puerto Rico." "Our fixed performance was led by 25,000 customer additions during the quarter as we strive to satisfy the significant demand in our markets for high-speed connectivity while typically bundling this lead product with our attractive video offering. We continue to invest in upgrading and expanding our networks with approximately 100,000 premises added in the quarter and we see potential to further upgrade and grow our footprint, generating healthy returns." Operating income (loss) was $139 million and ($206 million) in three months ended September 30, 2018 and 2017, respectively, and $361 million and $85 million for the nine months ended September 30, 2018 and 2017, respectively. These improvements were primarily driven by lower impairment, restructuring and other operating items, net, mostly due to impairment charges recorded during Q3 2017 to reflect the impacts of Hurricanes Irma and Maria.

Dividend Payers

Pattern Energy Group Inc. (PEGI) has released its financial results for the 2018 third quarter. Proportional gigawatt-hours (GWh) sold of 1,623 GWh, were up 7%; net cash provided by operating activities was $106.9 million; cash available for distribution (CAFD) was $31.7 million, up 235% and on track to meet full-year guidance; net loss was $31.5 million; adjusted EBITDA of $79.5 million, was up 45% on revenue of $118.4 million, up 29%. PEGI declared a fourth quarter dividend of $0.422 per Class A common share or $1.688 on an annualized basis, subsequent to the end of the period, unchanged from the previous quarter's dividend. During the period, the company committed to a plan to repower the 283-megawatt (MW) Gulf Wind project starting in 2019, acquired a 51% owned interest in the 143 MW Mont Sainte-Marguerite project in Quebec, for a purchase price of $37.7 million, representing a 10 times multiple of the five-year average CAFD of the project and completed the sale of the company's operations in Chile, which principally consist of its 81 MW owned interest in the 115 MW El Arrayan project for which Pattern Energy received cash proceeds of $70.4 million.

Economic Conditions

U.K. Consumer Spending grew +4.4% year/year in October 2018, according to the latest Barclaycard data. This comes in above both the three-month average (+4.2%) and 12-month average (+4.0%). The October data runs from September 23 to October 20, 2018.

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New Zealand's unemployment rate dropped significantly from 4.4% in the second quarter to 3.9% in the third quarter, against expectations for it to hold steady at 4.4%. This marks the lowest jobless rate since the second quarter of 2008, more than ten years ago.

Financial Conditions

U.S. - The Federal Open Market Committee (FOMC), as widely expected, kept its policy Fed Funds Target Rate (FFTR) unchanged at a 2.00%-2.25% range in a unanimous decision (9-0). Other than a slight downgrade in business fixed investments, the accompanying policy statement was largely verbatim from September's. The U.S. labour market has continued to strengthen and economic activity has been rising at a strong rate. The FOMC reiterated that it expects further gradual increases in fed funds rate will be consistent with sustained economic expansion, strong jobs market and inflation objective. This suggests that the FOMC is on track for a fourth rate hike in December in our view.

The Reserve Bank of Australia (RBA) held its official cash rate (OCR) at 1.5% during its November meeting. It last cut the OCR in August 2016, following an earlier cut to 1.75% in May. There has not been a rate increase since November 2010.

The Reserve Bank of New Zealand (RBNZ), as expected kept the OCR steady at 1.75%.

The U.S. 2 year/10 year treasury spread is now 0.26% and the U.K.'s 2 year/10 year treasury spread is 0.70% - 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 4.94% (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 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 17.95 (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.

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 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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