News Highlights

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PORTLAND INVESTMENT COUNSEL®

Our views on economic and other events and their expected impact on investments. November 28, 2016

Energy Sector

U.S. land rig count increased by 5 rigs to 568, marking the 21st week of gains in the last 26 weeks since the May bottom and the rig count is now up on average 21% quarter to date quarter/quarter. Gains in Horizontal Gas (+4), Directional Oil (+3), Horizontal Oil (+1), and Vertical Gas (+1) were partially offset by declines in Directional Gas (-3) and Vertical Oil (-1). Total horizontal land rig count is 65% down since the peak in November 2014. The Permian currently makes up 51% of all oil rigs.

U.S. horizontal oil land rigs increased by 1 rig to 376, as gains in the DJ-Niobrara (+2), Permian (+1), and Mississippian (+1), were offset by declines in Woodford (-2) and Williston (-1), while Eagle Ford, Granite Wash, and “Other” remained flat.

U.S. horizontal gas land rigs increased by 4 rigs week/week to 99 driven by the Marcellus (+4), which is the largest weekly gain in the Marcellus since March 2015.

U.S. Gulf of Mexico offshore rig count remained flat at 23 rigs and is down 57% since June 2014.

Canadian rig count decreased by 10 rigs and is down 6% from the level this time last year.

Baytex Energy Corp. has entered into an agreement to acquire heavy oil assets located in the Peace River area of Northern Alberta, for cash consideration of $65 million. The assets are located immediately adjacent to the company’s existing Peace River lands, add approximately 3,000 barrels of oil equivalent per day of production (boed) and more than double the company’s land base in the area. The acquisition is expected to close before year-end. The acquisition will be financed through a concurrent $100 million bought deal financing. The Peace River region has been a core asset for Baytex since the company commenced operations in the area in 2004. Through the company’s innovative multilateral horizontal drilling and production techniques, the area is recognized as having some of the strongest capital efficiencies in the oil and gas industry and, over the years, has contributed significantly to the company’s growth. The company sees the potential to significantly increase crude oil production from the acquisition over the next two years. Baytex is acquiring 415 net sections of long-tenure oil sand leases, which will more than double the company’s land position in the area. Prior to this acquisition, the company held 338 net sections of oil sand leases in the Peace River area. The acquired assets are currently producing approximately 3,000 **barrels of oil equivalent per day** (85% heavy oil) and are 100% operated. The acquisition will increase the company’s production at Peace River by approximately 20%. In addition, the acquisition includes approximately 3,000 boed that is shut in due to regulatory requirements and economics.

In connection with the acquisition, Baytex has entered into an agreement with a syndicate of underwriters, co-led by Scotia Capital Inc. and RBC Capital Markets, pursuant to which the underwriters have agreed to purchase, on a bought deal basis, 19.05 million common shares at a price of $5.25 per share to raise aggregate gross proceeds of approximately $100 million. The net proceeds will be used to finance the acquisition, reduce bank indebtedness and finance continuing capital expenditures.

Financial Sector

The Bank of Nova Scotia is reportedly in talks to sell HollisWealth, an independent adviser network, as the wealth-management industry faces slowing growth and greater regulatory pressure. Quebec City-based Industrial Alliance Insurance and Financial Services is the front-runner to buy the business. It isn’t clear how much Industrial Alliance is offering for the asset or if the process will result in a definitive sale. HollisWealth provides advisory services including investments, insurance, mortgages, tax services, estate planning and private banking. The firm’s network consists of about 800 advisers in more than 300 locations across Canada.

Citigroup Inc. has joined JPMorgan Chase & Co. at the top of global regulators’ list of systemically important banks, replacing HSBC Holdings Plc and meaning the U.S. bank will have to hold extra capital from 2019 to help preserve financial stability. In the annual update of rankings published last Monday by the G20’s Financial Stability Board (FSB), Citigroup has replaced HSBC in the top “bucket” facing a 2.5% capital surcharge on top of global minimum requirements. No lender joined or dropped out of the top 30 list this year. Four banks moved up a place. Citigroup rose to fourth, Bank of America Corporation moved up to third, and Industrial and Commercial Bank of China Ltd. and Wells Fargo & Company took second place. Meanwhile, three banks moved down a step. HSBC went from fourth to third, Barclays Plc and Morgan Stanley dropped to second. (Source: Reuters)

Citigroup said last Monday that it would increase its common stock repurchase program by up to $1.75 billion. The amount is in addition to the $10.4 billion in planned capital actions announced earlier this year, Citigroup said in a statement. Citigroup said it had reduced the number of its outstanding common shares by 180 million, or 6%, in the past two years. (Source: Reuters)

Royal Bank of Scotland Group Plc (RBS) - Clydesdale and Yorkshire Banking Group has confirmed it is in “ongoing” talks to acquire Williams & Glyn from RBS with the aim of boosting scale to compete in the retail and small business banking market. David Duffy, chief executive of the banking group, told the Financial Times that he believes Clydesdale is "the only true SME and retail challenger" in the market, adding, "We want to grow that in scale … grow and compete". RBS said earlier this year it would strike a "binding agreement" to sell Williams & Glyn by the end of 2016. It must fully divest the challenger bank by the end of next year, under EU rules for receiving a £45 billion taxpayer bailout during the financial crisis. Clydesdale reported its first annual pre-tax profit for five years last Tuesday, achieving £77 million for the 12 months to the end of September, reversing a loss of £285 million from the previous year. Clydesdale demerged from National Bank of Australia Ltd. earlier this year and listed on the London Stock Exchange. (Source: Financial Times)

Activist Influenced Companies

Restaurant Brands International Inc. – Burger King, a unit of Restaurant Brands International, plans to add 300 more stores in Germany over the next 6-7 years, its German head Andreas Bork told German weekly Welt am Sonntag. Bork says Burger King currently has around 700 stores in Europe's biggest economy.

Canadian Dividend Payers

Nothing new to report.

Global Dividend Payers

Johnson & Johnson – U.S. healthcare company Johnson & Johnson said on it is in preliminary talks with Actelion Pharmaceuticals Ltd. about a potential takeover of Europe's largest biotech firm, currently valued at about $20 billion. Lung disease specialist Actelion confirmed it had been approached and said there was no certainty a deal would occur. An acquisition of the Swiss company would boosts J&J's drug pipeline and diversify its prospects. J&J's biggest product, the arthritis drug Remicade, faces cheaper competition from Pfizer Inc. Actelion's focus on rare diseases makes it an attractive takeover target because drugs in that area are less prone to pricing pressure. J&J's chief executive, Alex Gorsky, said earlier this year that the company was interested in deals to expand its main consumer, medical device and pharmaceuticals segments. In September, J&J agreed to buy Abbott Laboratories' eye care business for about $4.33 billion in cash.

Actelion has long been seen as a takeover target. However, Actelion co-founder and Chief Executive Jean-Paul Clozel, who holds a 3.5% stake in the company, has repeatedly said he wants it to remain independent. In 2011, Clozel rallied shareholders against activist investor Elliott Management's campaign to put the biotech firm up for sale. Actelion's shares have more than tripled since then.

Economic Conditions

U.S. durable goods orders jumped 4.8% in October, much higher than expected, while September's decline was erased to reflect a 0.4% gain. So that's four straight months of improvement. But the headline is volatile; excluding transportation equipment, orders rose a more moderate but still solid 1.0%, also the fourth rise in a row (or 4.6% annualized over the past three months). By sector, the gains were widespread, with just primary metals, motor vehicles/parts and communications holding back a stronger gain. Excluding aircraft (which soared), orders dipped 0.2%. General machinery orders have yet to decline over a 6-month stretch, which suggests that capital spending on equipment should start to pick up.

U.S. – Consumer sentiment jumped higher in November, to 93.80 index points from 87.20 in October, ahead of the expectations for an improvement to a 91.60 index points level. Both the 'current conditions' and the 'expectations' components of this composite index advanced in the month.

Canada – Retail sales in Canada advanced by 0.6% in September, much as expected, driven chiefly by strong auto sales. Retail sales excluding auto sales were flat in the month, short of the expectations for a 0.5% improvement, with some of the weakness stemming from lower food prices.

Financial Conditions

The U.S. 2 year/10 year treasury spread is now 1.21% and the U.K.'s 2 year/10 year treasury spread is 1.29% - 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.

Influenced by the withdrawal of quantitative easing, the U.S. 30 year mortgage market rate has increased to 4.03% (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 4.8 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 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 13.42 (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 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 Focused Plus Fund
- 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

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