News Highlights

Owners. Operators. And Insightful Investors.

Phone: 1-888-710-4242
Web: www.portlandic.com
Email: info@portlandic.com

Established in 2007

PORTLAND INVESTMENT COUNSEL®

Our views on economic and other events and their expected impact on investments. September 30, 2019

Portland Product Call

REPLAYS of previous calls are available either at www.portlandic.com/advisors/

Username = Portland Password = pic1375 or: Clicking on the Advisor Log-In button at the top of the Portland website pages: www.portlandic.com

Owner Operated Companies

Carnival Corporation & plc – Cruise operator Carnival cut its 2019 profit forecast for the third time as it expects to take a hit from higher fuel prices. Fuel, a large part of cruise operators' operating costs, accounted for about 11.4% of Carnival's total operating expense in its third quarter ended Aug. 31. Oil prices surged recently following attacks on Saudi Arabia's biggest oil facility that has triggered geopolitical tensions in the Middle East. Chief Executive Officer Arnold Donald said he expects a hit of 8 cents per share from the recent spike in fuel prices. The company said it now expects adjusted earnings of $4.23 to $4.27 per share in 2019, down from its earlier forecast of $4.25 to $4.35 per share. The outlook overshadowed the cruise operator's better-than-expected quarterly sales and profit. Carnival's revenue rose nearly 12% to $6.53 billion, beating the average analyst estimate of $6.17 billion. Excluding extraordinary items, the company earned $2.63 per share, ahead of $2.53 per share estimated by analysts.

Energy Sector

Baytex Energy Corp. announced changes to its board of directors and management team. In the last year, the company has significantly restructured its board. Throughout this renewal process, the company's intent has been to create an efficient, diverse and independent board with complementary skill sets suited to its business. As previously highlighted, Baytex welcomed Jennifer Maki as a director on September 9, 2019. Kevin Olson has stepped down from the board of directors to concentrate on his other business ventures. Following a thorough review of its organizational capabilities, Baytex is streamlining its management team. Jason Jaskela, Executive Vice President and Chief Operating Officer, and Jonathan Grimwood, Vice President, Exploration are no longer with the company. Baytex's operating business units will now report directly to Ed LaFehr, President and CEO. Baytex continues to forecast 2019 average production of approximately 97,000 boed (83% oil and natural gas liquids) and expect to exit 2019 producing 95,000-97,000 boed. The company is forecasting exploration and development expenditures for 2019 of approximately $560 million.

Total S.A. held their Investor Day last week during which the company announced that it expects to grow dividends at 5-6% per annum beyond 2020 (twice the previous rate), does not plan any large-scale M&A and will return excess cash to shareholders through buybacks above $60 per barrel and will likely continue the current approximately $1.5 billion a year program out to 2025. Essentially the company is sharing the upside in cash flow that it is generating through the immediate dividend increase, rather than waiting to post 2020. The increase is the equivalent of about $500 million per year. Total expects to see global gas demand grow in excess of 2% per year with liquefied natural gas (LNG) growing even faster. The company sees natural gas liquids being greater than 15% in 2030 compared to 11% in 2018. Depending on the rate of growth the market could tighten as soon as 2020, although this is more likely to be 2021 onwards. Two-thirds of global LNG sales are still sold through long-term oil indexed contracts, but there is a clear trend towards commoditization. Total's integrated gas production is set to essentially double between 2019 and 2025 with the share of group production rising to 22% from the current 14%. Total is now supporting the ban on single-use plastics as they believe the current disposal approach is not acceptable. To that end, the group acquired Synova, a leader in automotive polypropylene recycling.

Financial Sector

Barclays plc last week announced two new additions to its Board (with deep experience in asset management), appointing: Mohammed el-Erian, the high-profile former CEO and co-CIO of PIMCO (he joins January 1, 2010); and Dawn Fitzpatrick, currently the CIO of Soros Fund Management, and previously a 25-year career within UBS O'Connor). These individuals add some international and asset management gravitas to the Barclays' board in our view, which has already seen a revamp this year, including the appointment of new Chairman Nigel Higgins. It will be interesting to see whether these new external perspectives bring any change to the entrenched strategy.

Rio Can Real Estate Investment Trust (REI), last week announced that its purpose-built rental project, eCentral, has leased up 72% of units at an average monthly rental rate of $3.88 per square foot. Management noted that both the velocity of leasing activity and the rental rates continue to be above expectations. Given the strength seen in the lease-up period, REI is consolidating its ownership position in eCentral. REI is purchasing the remaining 50% interest in the residential and retail projects. The total purchase price is $114 million, based on 1) cost plus $10 million for the residential piece; and 2) a 7%

cap rate for the retail piece. Management estimates the blended yield on cost at 5.3% on its projects at eCentral, driving close to $120 million of value creation (approx. $0.40 per unit), including the expected condo sales gains. REI has secured $150 million in financing to replace its construction facility with an 11-year term at a cost of capital of 2.58%. When the rental building has stabilized (which is expected in Q1 2020), the loan should become CMHC-insured and the cost of capital will drop to 2.33%. Also another $40 million in financing will be made available. At the end of Q2, REI spent $100 million of an expected $106 million on its 50% interest in the residential rental and retail components of this project. It is now spending another $114 million to consolidate the remainder. The condo project currently has $32 million in capital invested, which along with the profit, is expected to come back to REI before the end of 2019. Given the lower cost of capital available on residential projects, we are not surprised to see REI maximize the leverage employed on this investment (close to 70% on a loan-to-cost basis initially).

Activist Influenced Companies

Brookfield Business Partners L.P., together with its institutional partners, and Clayton, Dubilier & Rice (CD&R) today announced a definitive agreement for Brookfield to acquire half of CD&R's ownership interest in Brand Industrial Services (BrandSafway). As a result of the investment, Brookfield and funds managed by CD&R will each own approximately 45% of the company. BrandSafway management will continue to own a minority interest in the business. BrandSafway is a leading provider of infrastructure services to industrial and commercial facilities on a global basis. The company delivers scaffolding and other work access solutions, forming and shoring equipment, and numerous specialty industrial services to more than 30,000 customers in more than 30 countries worldwide. Its solutions support a wide range of global infrastructure ranging from refineries and petrochemical plants, to commercial buildings, bridges, hydroelectric dams, and other power facilities. Brookfield's investment will be funded with approximately $1.3 billion of equity. Brookfield Business Partners intends to fund approximately $400 million, with the balance being funded by institutional partners. The transaction is anticipated to occur in the first quarter of 2020.

Dividend Payers

Brookfield Infrastructure Partners L.P. announced the intention to create a Canadian corporation in order to provide investors with greater flexibility in how they access BIP's globally diversified portfolio of high-quality infrastructure assets. BIP intends to distribute to existing unitholders, on a tax-free basis, class A shares of the new corporation, Brookfield Infrastructure Corporation (BIPC). From an economic and accounting perspective, the transaction will be analogous to a unit split as it will not result in any underlying change to aggregate cash flows or net asset value except for the adjustment for the number of units/shares outstanding. Currently, unitholders are expected to receive 0.11 BIPC shares for each unit held of Brookfield Infrastructure in the form of a special distribution. The benefits of the creation of BIPC include potential enhanced demand from U.S. retail investors due to more favourable tax attributes, potential increased demand from institutional investors who are currently unable, or prefer not to, own partnership units, and the ability to qualify for further index inclusion, which is not available today.

Dufry AG - AENA SME S.A. has decided to extend Dufry's current duty-free contract covering 25 Spanish airports for up to 5 years. The contract will take effect after the expiry of the current agreement on October 31, 2020. Spain accounts for around 9% of revenue and is therefore an important contract. While the structure of the annual minimum guarantee has been amended, the variable concession fee component remains unchanged. The new agreement includes an average annual increase of 1.56% down from 6%. Assuming revenue growth of 3% (passenger growth of 5.7% in the first half of 2019), it is estimated EBITDA margin would increase from 4.8% in fiscal year 2021 to 7.8% in fiscal year 2025. Growth acceleration in Spain should come from the rollout of the successful commercial initiatives tested across five pilot airports since June 2018. These initiatives include: 1) optimization of shop sizes and locations; 2) capturing passenger flow through walk-through shops; and 3) pricing, product assortment and brand optimization.

Prudential Financial, Inc. has sweetened the terms of its imminent demerger of M&G Investments by promising a £100 million one-off dividend to investors in its newly independent investment business. The UK's largest insurance company announced last Wednesday that asset manager and insurer M&G would be spun off into a separate Financial Times Stock Exchange 100 index company by October 21 - 10 days before the UK is due to leave the EU. M&G will not raise new capital via the transaction; instead existing Prudential shareholders will effectively receive one M&G share for every group share they own. In an added one-off bonus for shareholders, M&G said it expected to pay a special dividend of about £100 million next year, equivalent to £3.85 per share. M&G chief executive John Foley brushed off concern over the proximity of the demerger to a potentially chaotic no-deal Brexit at the end of October, noting that the political uncertainty could continue after that time. There was an update on current trading and prospects (focused on new business sales) for both Prudential plc and M&GPrudential. In short, current trading is broadly unchanged from the August 1H2019 earnings call, except the impact of the Hong Kong disruption on new business sales there (recent press articles have suggested that the geopolitical tensions have impacted cross-border sales). There was also some commentary on the effect of lower yields on solvency metrics. Putting together anticipated dividends (including a special demerger dividend to M&GPrudential), the total dividend is expected to grow 5% on what Prudential paid out in 2018. One-time demerger costs are guided to be £350 million in total pre-tax, of which about 65% spent in 1H2019, and the rest to be taken in 2H2019.

Phone: 1-888-710-4242
Web: www.portlandic.com
Email: info@portlandic.com

In addition, there will be annual recurring costs of £80 million-£100 million for the group from extra head office and group function expenses.

WPP plc has hired Unilever's former marketing chief as a non-executive director. Keith Weed, who will join in November, oversaw campaigns for brands such as Dove soap, Knorr condiments and Lipton tea until May this year when he retired after 35 years at Unilever. "Keith is one of the world's most influential and successful marketers" said Roberto Quarta, WPP chairman. "He has a deep understanding of our business, the ways in which technology is transforming marketing, the sectors in which we operate and our fast moving consumer goods clients in particular."

Economic Conditions

U.S. personal spending slowed in August, rising 0.1%, with volumes up similarly but after a downward-revised 0.3% advance the prior month. Consumer spending could still top 3% annualized in Q3 2019 (after 4.6% in Q2 2019), but this will require a moderate gain in September. That seems likely given solid income support. Personal income rose an expected 0.4%, keeping the yearly rate above 4.5%. Note that real income is up 3.0% in the past year, fully supporting the 2.3% advance in real consumer spending. Also note that real spending on highly discretionary recreational goods and vehicles rose another 1.0% in August, taking the 8-month run up to a 25.7% annualized rate, the fastest pace since the credit boom of the early 2000s. Core prices rose a light 0.1% (0.14%, despite a 0.3% pop in core consumer prices). This limited the upturn in the yearly rate to 1.8% (1.77%) from an upward-revised 1.7% in July. While the yearly pace is still below the Fed's 2% target, the shorter-term metrics are perched above it (2.5% for three months and 2.1% for six months).

U.S. Conference Board - consumer confidence fell 9.1 points (largest drop since December) to a 3-month low of 125.1, as worries about the present situation (-7.0 points to a 3-month low of 169.0) were compounded with fading hopes for the future. Expectations slumped 10.6 points (most since December) to an 8-month low of 95.8.

India announced surprise corporate tax cuts. Following major elections earlier this year that saw PM Narendra Modi hold onto power, providing political continuity in the world's largest democracy, another catalyst emerged last week. India's government introduced a new corporate tax schedule that ushered in new, lower rates that should be accretive for growth. The headline corporate tax rate was reduced 8% from 30% to 22%, thereby providing stimulus of roughly $20 billion to the economy. Further, a new special tax rate of 17% was implemented for companies starting new manufacturing facilities until 2023, which should support foreign direct investment as well as domestic private investment. The government also removed an additional surcharge on capital gains taxes, which could help support additional investment in Indian stock markets. We believe that the tax cuts should help boost corporate savings and the private sector investment rate – both measures that have previously proven headwinds to economic growth. Also, continued privatization of public sector firms should help drive capital return for the government.

Financial Conditions

The Reserve Bank of New Zealand (RBNZ) held its official cash rate (OCR) unchanged at 1.00%. In its accompanying press release, the RBNZ began by saying that "new information since the August Monetary Policy Statement did not warrant a significant change to the monetary policy outlook." The RBNZ's decision to stay put at this meeting was not surprising given the bigger-than-expected move back in August, which we deemed as pre-emptive in nature. That said, the RBNZ is clearly on an easing bias, and expects interest rates to remain "low for longer" to help support the Kiwi economy.

The U.S. 2 year/10 year treasury spread is now 0.0502% and the U.K.'s 2 year/10 year treasury spread is 0.113% - 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 2 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 3.64% (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 6.4 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 15.35 (compares to a post-recession low of 17.23 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.

Phone: 1-888-710-4242
Web: www.portlandic.com
Email: info@portlandic.com

September 30, 2019

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 Fund
- 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) per unit 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.

Portland Investment Counsel Inc.   portlandinvestmentcounsel   Portland Investment Counsel Inc.   @PortlandCounsel

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, 'GDP' gross domestic product, 'netback' is a measure of oil and gas sales revenues net of royalties, production and transportation expenses and is used to compare performance in the oil and gas industry, 'ROE' return on equity, 'ROTE' return on common equity, 'ROTCE' return on tangible common equity.

Portland Investment Counsel Inc., 1375 Kerns Road, Suite 100, Burlington, Ontario L7P 4V7 Tel.:1-888-710-4242 • www.portlandic.com • info@portlandic.com

PIC19-057-E(10/19)