

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.

April 13, 2020

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Owner Operated Companies

Apple Inc. and Alphabet Inc.'s Google said that they will work together to create contact tracing technology that aims to slow the spread of the coronavirus by allowing users to opt into logging other phones they have been near. The rare collaboration between the two Silicon Valley companies, whose operating systems power 99% of the world's smartphones, could accelerate usage of apps that aim to get potentially infected individuals into testing or quarantine more quickly and reliably than existing systems in much of the world. Such tracing could play a vital role in managing the virus once lockdown orders end. The companies said they started developing the technology two weeks ago to streamline technical differences between Apple's iPhones and Google's Android. Under the plan, users' phones with the technology will emit unique Bluetooth signals. Phones within about six feet can record anonymous information about encounters. People who test positive for the virus can opt to send an encrypted list of phones they came near to Apple and Google, which will trigger alerts to potentially exposed users to seek more information. Public health authorities would need to sign off that an individual has tested positive before they can send on the data. The logs will be scrambled to keep infected individuals' data anonymous, even to Apple, Google and contact tracing app makers. Apple and Google said their contact tracing system will not track GPS location. Apple and Google plan to release software tools in mid-May to contact tracing apps that they and public health authorities approve.

Danaher Corporation announced that for the quarter ended April 3, 2020 it expects revenue growth of approximately 3.0% and non-GAAP core revenue growth of approximately 4.5%. President and CEO Thomas P. Joyce, Jr. said, "We anticipate positive results in each of our three reporting segments in the first quarter, with particular strength in our Cepheid, Radiometer, Pall and ChemTreat businesses. While we had a good start to the year, we saw a meaningful slowdown in demand toward the end of the quarter, particularly in our more instrument-oriented businesses, as the COVID-19 pandemic spread worldwide." Joyce continued, "We are incredibly proud of our team's response to these unprecedented challenges. We are directly contributing to the fight against this virus, providing much-needed diagnostic testing capabilities and supporting our customers in pursuit of new treatments and vaccines." Due to the evolving and uncertain impact of the COVID-19 pandemic, Danaher also announced that it is withdrawing its previously communicated 2020 financial guidance, which was provided on January 30, 2020.

Walgreens Boots Alliance, Inc. is launching 15 "drive-thru" testing sites for coronavirus infections, as it follows up on a pledge it made to work with the Trump administration on expanding diagnostic centres. Like CVS Health Corporation, which said it was launching two offsite testing locations, Walgreens will also use Abbott Laboratories' faster test kits, allowing the drugstore chain to do 3,000 tests per day across the sites. CVS had said it would be able to handle 1,000 tests per day. Abbott's tests deliver results in as little as five minutes and negative results within 13 minutes, Walgreens said, adding that it would set up centres in Arizona, Florida, Illinois, Kentucky, Louisiana, Tennessee and Texas.

Energy Sector

Oil output cuts – The Organization of the Petroleum Exporting Countries (OPEC) and allies led by Russia agreed to reduce output by 9.7 million barrels per day (bpd) in May and June - equal to nearly 10% of global supply. The cut by OPEC+ may be more than four times deeper than the previous record set in 2008 and overall oil supply may shrink by twice that with other measures, but the reduction falls short of a demand drop predicted by some forecasters to be as much as 30 million bpd in April.

OPEC producers and allies including Russia and USA have agreed to a record oil deal that will substantially reduce global oil output by about 10% starting May 1st. However as the coronavirus lockdowns are estimated to have reduced consumption by over 30% as more than 3 billion people are staying at home it would seem the impact is likely to prove muted.

Saudi Energy Minister Prince Abdulaziz bin Salman said that G20 nations had pledged to cut about 3.7 million bpd and that strategic reserves purchases would reach roughly 200 million barrels over the next couple of months, bringing the total reduction of oil in the market to about 19.5 million bpd. Big producers such as Canada, Norway and the United States have yet to commit publicly to fixed quotas.

Canada's Oil Sands are suffering the double blow of the coronavirus pandemic and the Russia-Saudi price war. The price war "is going to ruin a lot of people's livelihoods, destroy countless small businesses and inflict a lot of pain" Jason Kenney, Alberta's premier, told The Financial Times.

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Financial Sector

JPMorgan Chase & Co.'s CEO, Jamie Dimon, last week said he sees a "bad recession" in 2020, and that the largest U.S. bank could suspend its dividend if the coronavirus crisis deepens. Dimon, widely regarded as the face of the U.S. banking sector, is the most prominent voice on Wall Street so far to project that the economic cost of the coronavirus will not evaporate quickly, and said the bank's earnings will be down "meaningfully in 2020."

Activist Influenced Companies

Nothing significant to report.

Dividend Payers

Nothing significant to report.

Economic Conditions

Canadian employment fell by more than 1 million in March (1,010,700 to be exact) according to the Labour Force Survey, much weaker than consensus expectations which were at about half that tally. That pushed up the unemployment rate by 2.2 percentage points to 7.8%, the biggest one-month jump since 1976. The participation rate fell 2 percentage points to 63.5%. Job cuts were driven by the private sector (-830,000), although there were also sharp declines in the public sector (-144,600) and in self-employment (-36,000). Employment in the goods sector fell 47,000 with losses in most categories including manufacturing and construction. Services-producing industries saw employment drop by 964,000 courtesy of declines in all categories including -294,000 for accommodation/food services.

Full time employment dropped 474,000 while the ranks of part-timers shrank 536,000. The jobs purge not surprisingly caused hours worked to sink 15% in March.

The option to work from home, because of the pandemic, is not available to a large part of the workforce and as such the largest job declines registered in March were in industries where employees had limited ability to work from home. The historic jump in the jobless rate would have been even steeper were it not for the slump in participation rate. This is unfortunately not the end of bad news for the Canadian labour market with further job losses in the cards despite the federal government's best efforts to encourage the private sector to keep its workers (via a range of programs including wage subsidization). All told, this is by far the largest and fastest pace of jobs decline ever recorded and confirms what everybody knew (even before GDP data is available), i.e. Canada is now in a deep recession.

The number of Americans filing for Unemployment Insurance (UI) for the first time slipped for the first time in about a month but considering that total initial filings were still a towering 6.606 million in the week of April 4, the 261,000 decline was barely noticeable in analysts' view in the grand scheme of things. Those who remain on UI (continuing claims) surged 4.396 million to 7.455 million in the last week of March, clearly a record. This stretch of UI claims measured in the millions is not going to end in the next few weeks. The lockdowns/social-physical distancing are having a huge hit on the U.S. economy and labour market. The backlog of filings at the UI offices, reports that some unemployment offices have people lined up outside to apply for benefits, shows how stressed the system is.

Germany and France enter recession. Germany's economy is set to shrink 1.9% in the first quarter and will shrink by 10% in the 3 months to June according to forecasts published last week by the country's top economic research institutes. In France, the shutdown is knocking 1.5% off French growth for every 2 weeks it continues, the Banque de France warned last week. (Source: Financial Times)

Financial Conditions

The Federal Reserve unexpectedly announced a huge \$2.3 trillion of support to backstop Main Street last week.

European Union finance ministers agreed last week to approve a stimulus plan to spend Euro 540 billion to lift their economies but as yet can't agree to take the unprecedented step of issuing joint bonds which would alleviate the worst-hit members like Italy and Spain. (Source: The New York Times)

The U.S. 2-year/10-year treasury spread is now 0.52% and the U.K.'s 2-year/10-year treasury spread is 0.27% - 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 3.33% (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 3.1 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.

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The VIX (volatility index) is 42.95 (compares to a post-recession low of 18.00 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...Daily carbon dioxide emissions have fallen about 58% across the EU since coronavirus lockdowns put the world economy into reverse and so reduced the human impact on the environment, according to calculations by Sia Partners, a French consultancy specializing in energy. Emissions from cars and motorcycles were down 88% while those from the energy sector fell almost 40% from before the crisis. (Source: Financial Times)

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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, '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 tangible equity, 'ROTCE' return on tangible common equity.

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