



News Highlights

Financial Services Companies

BNP Settlement Terms (with Federal Reserve, Dept of Justice, NY Attorney General): \$8.97bn cash fine: - Some tax deductibility depending upon each jurisdiction's tax laws plus guilty plea to charges of falsifying business records and conspiracy. USD suspension to begin January 1, 2015 and lasting for 12 months. Suspension applies to oil and gas transactions from Geneva, Paris, Singapore and Rome offices and trade finance from Milan office. For this period trades are to be managed via a third party (BNP Fortis already uses a third party). Additionally, BNP will not serve as a dollar-clearing correspondent bank for other New York and London-based lenders for two years. Transactions completed in violation of US sanctions totaled \$9bn from 2002-2012 (\$0.9bn Cuba, \$1.7bn Iran, \$6.4bn Sudan). Transactions included \$6.4bn in 12 months for Sudan during 2006-7 with NY AG indicating BNP "acting in essence as the central bank of Sudan" However, BNP will NOT be barred from serving as an investment adviser. NYS regulator forcing 13 employees to leave, including COO Courcel, ex-head of compliance Garboua, ex-head of CIB structure finance Remy, and North America head of compliance Strombelline and 45 employees disciplined

BNP trading Update, post the fine: keeping with existing three year plan (oil and gas are 1% group revenues); a Eur 5.8bn Q2 charge (\$7.9bn ex-\$1.1bn existing reserve). Still paying a Eur 1.50/sh cash dividend for 2014 (unchanged). 2014Q2 core Tier 1 equity capital ~10% with flat Risk Weighted Assets compared to Q1 of 10.7% and 2014Q2 leverage ratio >3% vs. Q1 3.7% And so BNP has managed absorb this large fine of USD8.97bn and still claw its Core Equity Tier 1 capital back to ~10% and committed to a €1.50 FY14 cash dividend.

BNP - S&P affirmed its 'A+' long-term credit rating on BNP Paribas on Thursday. S&P said it revised its assessment of the bank's capital to "moderate" from "adequate".

Citigroup Inc has bought Deutsche Bank AG's U.S. power trading books, the latest move by the U.S. bank to build its energy trading business as other Wall Street rivals retreat.

Deutsche sold two power trading books to Citi last week covering the ERCOT region in Texas and the East and Midcontinent. The Deutsche sale to Citi as part of the closure of its energy trading business was first reported by trade journal SparkSpread (Source: Reuters).

Goldman Sachs (and Barclays) - Financial Industry Regulatory Authority (FINRA) announced last Wednesday that it has fined Goldman Sachs Execution & Clearing, L.P. \$800,000 for failing to have reasonably designed written policies and procedures in place to prevent trade-throughs of protected quotations in NMS stocks from Nov 2008 through Aug 2011 in connection with trading in its proprietary alternative trading system, SIGMA-X. The Order Protection Rule generally requires that trading centers trade at the best-quoted prices or route orders to the trading centers quoting the best prices. FINRA found that from July 29, 2011, through Aug 9, 2011, there were more than 395,000 transactions executed in SIGMA-X where the execution traded through a protected quotation at a price inferior to the National Best Bid and Offer (NBBO). In connection with the approximately 395,000 trade-throughs, Goldman Sachs returned \$1.67mn to disadvantaged customers. In settling this matter, Goldman Sachs neither admitted nor denied the charges, but consented to the entry of FINRA's findings. Not sure where Goldman Sachs' failure (to ensure that trades executed in the bank's own dark pools met investors' right to best market prices) leaves the c£2bn knocked off Barclays market cap on last week's announcement of US investigation into dark pool activity, but should be seen as mildly positive. (It is very difficult to fathom the regulators approach e.g. in sanctions space BNP were fined \$9bn whereas RBS \$100m without obvious analysis re difference). Whilst size of exposures is easier to analyze, potential outcomes remain more uncertain.

HSBC - are set to close its Libyan operations as it reviews businesses. CEO Stuart Gulliver is seeking to simplify the bank's structure and boost returns by selling assets and focusing on growing economies in which the bank has the greatest market share.

ING - Announcement on the IPO of its insurance arm NN Group - the IPO was priced at EUR20, with an implied valuation of NN of EUR7bn, middle of the initial indicative range of EUR6.5bn-8bn. ING actually exercised the over-allotment option, increasing the share offering from 70mn to 77mn - so while the pricing



wasn't at top end, there was clearly sufficient demand for the stock. In Q1, NN made a profit of EUR274mn (ongoing basis), so the deal was priced at c9x annualised earnings, which seems reasonable for a mature Dutch insurance book. ING still holds 71% of NN, but will plan to sell it down to below 50% before end of 2015, and the rest in 2016. ING will receive EUR1.5bn from the IPO, and this will be used to reduce the double leverage of the group, but will have a negative accounting impact of EUR3.4bn on ING's equity base. ING made it clear that it plans to start paying a dividend only in 2015. This is all part of the restructuring programme as agreed with the state aid requirement. ING has a market cap of EUR40.4bn currently - the bank has book value of EUR33bn with ROE of 10-11%, so 1x book gives EUR33bn, adding the valuation of the insurance group. Shares in the insurer NN leapt 6.3% in their debut trading session. The rally added another €40m to NN's market capitalisation after the Amsterdam listing valued its equity at €7bn.. The successful stock market launch is a milestone in the recovery of ING, the financial services group forced to dispose of the insurer after it was bailed out by the Dutch state during the financial crisis.

JP Morgan: CEO Jamie Dimon disclosed in an 8-K last Tuesday that he has been diagnosed with throat cancer which appears to have been caught early, hasn't spread and is curable according to his medical team. Radiation/chemotherapy treatment is expected to take 8 weeks. While the treatment will curtail his travel during this period, he has been advised that he will be able to continue to be actively involved in JPM's business, and will continue to run the company as normal. I wish him the best and hope he returns to good health quickly. There are few bankers that can successfully run a company as complex as JPMorgan and Jamie Dimon certainly has the pedigree and proven he can do it. But, unfortunately, it's likely over the next few months, this issue will serve as an overhang on the stock. Inevitably, the question will arise as to much in the "tank" does Jamie have left. The crisis wasn't easy, the Whale left a mark and now he is dealing with the a personal health issue so I think it is logical to ask "who is next in line"? The short list for possible successors includes D. Pinto, CEO of the Corp. and Investment-Bank and Gordon Smith, CEO of Consumer or even potentially COO Matthew Zames.

Lloyds Bank / Bank of America - The treasurer of Lloyds, Andrei Magasiner, is leaving Lloyds to become the CFO of the Global Markets and Global Banking division at Bank of America, press reports according to people familiar with the matter. Magasiner

was regarded very well internally and externally at Lloyds, and was accredited with largely being responsible for getting the funding profile of the bank in shape.

Morgan Stanley has bought Deutsche Bank's bulk commodities trading book dealing in coal, iron ore and freight forward contracts to expand in commodities derivatives, a source familiar with the matter said on Thursday. The deal marks an apparent return to iron ore for Morgan Stanley, which exited the market by last year, and an expansion in coal and freight. The size of the book is not known, although Deutsche was one of the pioneers of iron ore swaps trading in 2008. The bulk commodities book is one of 17 put up for sale by Deutsche as part of its decision to exit commodities trading because of toughening regulations and diminished profits (Source:Reuters).

Dividend Payers

Novartis' hopes of negotiating Glivec generic risk through switching patients to the more potent Tasigna took a blow when Novartis was forced to pull Tasigna's filing for a label extension in Europe to cover treatment of patients in whom Glivec had failed to produce a full response after it became clear the regulator was unlikely to recommend Tasigna approval based on the existing data. The regulator says this was because the study failed to demonstrate treatment with Tasigna significantly increased the percentage of patients who had a complete molecular response by 12-months. It was also unclear how a complete molecular response would translate into an improvement in patient outcome. This raises a deficiency in Novartis' strategy to protect its Glivec franchise from generic competition, which in the long-run may restrict Tasigna market penetration in the face of Glivec generics. Thus, although Novartis has demonstrated rates of major molecular responses and complete cytogenic responses are greater in patients treated with Tasigna compared to Glivec, in newly diagnosed patients with chronic myeloid leukaemia, whether this translates into improved survival, in our view, remains an unknown.

Roche has announced a definitive agreement to acquire the US biotech Seragon Pharmaceuticals to gain access to the latter's novel approach to the treatment of hormone positive breast cancer. About 60% to 75% of breast cancers are supported by oestrogen and progesterone and approaches targeting this pathway, notably the oestrogen receptor blocker tamoxifen and the aromatase inhibitors (of oestrogen synthesis), have proven very effective in the treatment of this form of breast



cancer. Seragon adds a third approach to disrupting this pathway, targeting both blockade of the oestrogen receptor (a la tamoxifem) and elimination of the oestrogen receptor from the cell altogether. Seragon's lead candidate, ARN-810, is in phase I clinical trials which makes the \$1.7bn deal (\$725m up front, \$1bn in milestones) a sizable bet on Seragon's selective oestrogen receptor degraders evolving into the next generation of drugs for the treatment of hormone receptor positive breast cancer. Little to nothing is known of the ability of ARN-810's ability to induce tumour regression or prolong survival without disease progression in patients with hormone refractory breast cancer or how it measures up against alternative approaches such as mTor inhibition (Afinitor, Novartis) or cell cycle arrest (palbociclib, Pfizer). As an aside, Roche's target window of net-debt to total assets of 0% to 15% suggests we can expect Roche to strike \$5bn plus in bolt-on deals each year. It seems unlikely any will be near-term price movers. Deals announced so far this year total upfront cash of \$850m.

Serco: trading is on course to hit the more recent guidance of not less than £155million of adjusted profit. Leverage is where it was expected to be, at 3x EBITDA. Flat organic growth for the period with margins' significantly lower' than what was earlier expected (halved). The bottom line is that there's no further warning here. The main incremental news is that further investigation into problem contracts as part of the strategic review has revealed larger issues than previously thought on two particular contracts – COMPASS (accommodation and support services for asylum seekers) and Suffolk Community Healthcare. The Suffolk contract is going to require a larger provision, although that is below the line as Serco is looking to exit the work. The loss-making COMPASS contract is now expected to remain that way over its full duration, meaning an onerous contract provision will be required. It is still to be determined whether it will be above or below the line, the decision being based on the size of the provision, as, for relationship issues, this will not be exited. Given the guidance has been reiterated, it seems some of the contingency was previously factored in but not being large enough to compromise the £155m figure. Overall, remaining on track is probably a positive. Serco trades on 18x 2015 estimate PE, falling to 15x 2016estimates, the latter in-line with its average over the last 5-years, albeit one-year further out. This balances margin recovery potential vs. revenue and execution risk in our view.

Seven & I Holdings : 1 Q results show Operating Profit rose 5.1% (or JPY3.8bn) YoY to JPY77.5bn in 1Q FY2/15, compared

with the Bloomberg consensus forecast of JPY76.5bn. Management left full-year guidance unchanged, but 1Q progress looks slightly ahead of target. The firm performance was mainly due to a better-than-expected contribution from the convenience store business thanks to brisk sales of products including private brands developed in conjunction with manufacturers. Sales of Seven Premium branded lines increased around 30% YoY to JPY194bn in 1Q, marking steady progress toward a full-year target of JPY800bn. The 5.1% (or JPY3.8bn) increase in consolidated OP breaks down mainly to positive contributions of +JPY6.0bn from the convenience store business (+JPY6bn at Seven-Eleven Japan, ±JPY0bn at 7-Eleven, Inc.), +JPY860mn from the department store business, and +JPY100mn from the superstore business (+JPY200mn at Ito Yokado, -JPY200mn at York-Benimaru) and negative contributions of -JPY300mn from financial services, and -JPY2.2bn from the mail order business (newly consolidated Nissen). Nissen struggled because yen depreciation pushed up CoGS. The situation should improve when the subsidiary launches products that factor in these increased costs, which are currently in development. The convenience store business's firm performance was not solely due to last-minute demand ahead of the consumption tax hike; a detailed pricing strategy and sales initiatives also helped to damp the consequent slump in demand in April. The company opened 398 stores, in line with its full-year target of 1,600. Same-store sales increased just 1.0%, compared with a full-year target of 2.3%, due to the impact of a harsh winter. Management believes fundamental progress is solid if one-off factors such as the weather are stripped out.

Siemens sells Steinmüller Engineering to IHI. Steinmüller Engineering is a process engineering group focusing on energy and environmental technologies. The group covers all aspects from design, construction and operation. Since 2012 this fully owned Siemens business has formed part of the Service area of the group. Employing a workforce of 90, this is a small business (sales not disclosed). IHI is a broadly diversified Japanese engineering group. This is another example of Siemens' ongoing efforts to streamline its portfolio.

Toyota did not disclose 1Q guidance, but gives the impression to expect Operating Profit to be below 1Q last year (JPY663.4bn). The company expects global retail sales of the three brands (Toyota + Lexus + Scion) to rise by approximately 40,000 vehicles YoY (1Q FY3/13: 2.233mn vehicles). However, the company expects consolidated sales volume to be below the level in the same period last year of 2.232mn vehicles.



By region, the company's view on retail sales is for a backlash to the demand rush ahead of the consumption tax increase in Japan (-30,000 vehicles YoY), but for growth overseas (+70,000 vehicles). Overseas, Toyota apparently expects declines in Oceania (-10,000 vehicles) and Asia (-30,000) but sees an increase in North America (+70,000) and the Middle East (+20,000), for upbeat growth overseas on the whole. As for sales volume, the company sees adverse weather conditions in North America since April pushing down production and shipments. For recall expenses arising from defective air bags (which other firms in the industry are also incurring), after calculating the costs on automaker side (as the other firms are doing), Toyota plans to reverse reserve provisions as the recall progresses and the allocation of the costs between the airbag supplier and the company is worked out. However, in Toyota's case, management expects reserve provisions to be within the normal amount, so it seems that additional reserves will be unnecessary.

Economic Activity, Consumer and Business Conditions

U.S. employment: in June, nonfarm payrolls jumped 288k in the month, the second largest increase since January 2012 and well above the YTD average of 230k. and the revisions are also up for May from 217k to 224k, and April from 284k to 304k! The private sector added 262k, the fifth consecutive month of +200k gains. The household survey of employment, a more volatile measure, jumped 407k in June and, along with an 81k rise in the labor force, took the jobless rate down 0.2% to a lower-than-anticipated 6.1%, the lowest since September 2008. The all-in jobless rate (officially known as U6) hit a near 8-year low of 12.1%. The # of discouraged workers fell for the second straight month. The average duration of unemployment also fell for the 4th month in a row to a near 4-year low of 33.5 weeks. Average hours worked rose 0.2%, and was up at a 3.8% for all of Q2. This suggests Q2 GDP growth estimates will be revised back up. Also good news was the 0.2% rise in average hourly earnings, the second such gain in a row although it was steady-ish at 2% above a year ago. Nothing too inflationary about that.

U.S. nonmanufacturing ISM : did come in roughly in line with expectations of 56.0 in June from 56.3 in the prior month. But similar to its manufacturing cousin, behind the headline dip were some stronger underlying details. All of the setback was in production or current activity (but still well >50) while new orders

edged up 0.7 pts to a 42-month high of 61.2), which bodes well for future production, and employment grew 2 pts to 54.4 (confirming the non-farm payrolls boost), and supplier deliveries slowed (up 1 pt to 51.0).

US Housing : For the third month in a row, more buyers signed on to buy a home across the U.S.A. in May. These contracts will eventually translate into an existing home sale in a month or two, depending if financing clears, and other issues that may crop up before such a contract closes. These contracts, also known as pending home sales, jumped 6.1% in May, totally bypassing expectations (of a 1½% rise) and was the largest monthly increase since April 2010, bringing the index to its highest level since last September. Sales are still 5.2% below a year ago but the movement in the past three months indicates that the sector continues to put the horrid weather behind it and is moving on. It certainly helps that confidence is higher and it is reportedly becoming less strenuous to obtain a mortgage. The rise was seen in all four corners of the country led by the Northeast (+8.8%), the West (+7.6%), the Midwest (+6.3%) while the South trailed (+4.4%).

ECB kept interest rates unchanged at record lows with the main refinancing rate kept at 0.15%.

EU integration: Ukraine, Georgia and Moldova have signed integration agreements with the EU as the EU also warns Russia that it risks further sanctions unless it takes concrete steps towards securing a peace deal in the east of Ukraine.

Sweden: The central bank cut its main interest rate by a more-than-estimated 0.5% and predicted no increases until the end of next year to shield the largest Nordic economy from deflation. Repurchase rate was reduced to 0.25% and the deposit rate to minus 0.5%. Negative for margins (Nordea/Swedbank) but should be good for economy (struggling with deflation) - i.e. like a profitable periphery.

Financial Conditions



US: US Federal Reserve policymakers remain determined to flatten the yield curve as much as possible, having indicated they expect 'exceptionally low levels of interest through 2014 with the Federal Reserve carefully calibrating the beginning of unwinding quantitative easing and undertaking that the Federal Reserve will keep rates low until mid 2015. The U.S. 2 year/10 year treasury spread is now 2.11% and the U.K.'s 2 year/10 year treasury spread is 1.84% - 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. It seems the top tier 6-9 investment banks will continue to command their market and possibly increase their share – as barriers to entry for newcomers have in our view been raised.

Influenced by the withdrawal of quantitative easing, the U.S. 30 year mortgage market rate has increased to 4.12% - (was 3.31%, end of November 2012 the lowest rate since the Federal Reserve began tracking rates in 1971), as the Federal Reserve effectively continues to give priority to incentivising home ownership. Existing U.S. housing inventory is at 5.2 months supply of existing houses. So the combined effects of low mortgage rates, near record high affordability, a more promising 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 11.06 (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 currently offers 5 mutual funds:

- Portland Advantage Fund
- Portland Canadian Balanced Fund
- Portland Canadian Focused Fund
- Portland Global Banks Fund
- Portland Global Income Fund
- Portland Global Dividend Fund

Private/Alternative Products

Portland also currently offers 3 private/alternative products:

- Portland Focused Plus Fund LP
- Portland Private Income Fund
- Portland GEEREF LP

Net Asset Value:

At the close of business each day we publish the Net Asset Values (NAV) of our mutual funds onto our Portland website at <http://www.portlandic.com/prices/default.aspx>

Closed-End Fund

Spreads on the closed-end fund remain, in our view, very attractively priced to purchase.

The Portland Investment Counsel's 2013 Fourth Quarter Fund update is now available on the website.

At the close of business each day we publish the Net Asset Values (NAV) of our funds onto our Portland website at <http://www.portlandic.com/prices/default.aspx>

The price details published are replicated here below from which you can see we also highlight whether the funds share prices are trading at a premium or discount to their respective NAV.

Market Commentary



PORTLAND
INVESTMENT COUNSEL®

July 7, 2014

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Source: Thomson Reuters, Bloomberg, Company reports

Certain statements included in this document constitute forward-looking statements, including those identified by the expressions “anticipate,” “believe,” “plan,” “estimate,” “expect,” “intend” and similar expressions to the extent they relate to the Fund. The forward-looking statements are not historical facts, but reflect the Portfolio Management team’s current expectations regarding future results or events. These forward-looking statements are subject to a number of risks and uncertainties that could cause actual results or events to differ materially from current expectations. The Portfolio Management team has no specific intention of updating any forward-looking statements whether as a result of new information, future events or otherwise. PORTLAND INVESTMENT COUNSEL and the Clock Tower Design are registered trademarks of Portland Holdings Inc.

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