Market Commentary

PORTLAND INVESTMENT COUNSEL®

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News Highlights

Energy Sector

Suncor Energy, Canada's largest oil and gas company, reported fourth-quarter profit lower by roughly 80%, hit by the rapid slide in oil prices and weaker output from its Alberta oil sands operations. Struggling to cope with oil prices that have fallen by more than half since June, Suncor last month laid off 1,000 staff and contractors, deferred some oil sands projects and slashed $1 billion from its capital-spending budget. The world's largest oil sands producer said quarterly net income fell to $84 million or $0.06 per share, down from $443 million or $0.30 in the same quarter a year earlier. Operating earnings, which excludes most one-time items, fell 60% to $386 million, or $0.27 per share, from $973 million, or $0.66. Suncor said output from its northern Alberta operations fell 6% to 384,200 bpd as unplanned maintenance at its project site hampered operations. Production costs fell to $34.45 from $36.85 per barrel in the year-prior quarter. The company produced a total 557,600 barrels of oil equivalent per day (boepd), down slightly from 558,100 boepd in the fourth quarter of 2013. Cash flow, a key indicator of the company's ability to pay for new projects and drilling, fell to $1.49 billion, or $1.03 per share, from $2.35 billion or $1.58 per share.

Financial Sector

Aflac reported 4Q14 operating EPS of $1.29 versus consensus of $1.28. The quarter was notable for robust third sector sales growth in Japan of 27%, led by cancer sales +176%. Additionally, the US also showed sales growth for the first time in five quarters.

BNP Paribas reported a 4Q14 PBT 1% ahead of consensus. Cost & Provisions better. Operating profit +12% vs consensus. Retail overall better but French retail some 10% below consensus. Corporate & Investment Bank miss in equities, beat in FICC. Capital 10.3% Fully Loaded Core Equity Tier 1 10.1% and confirmed dividend at €1.5. They guide to €340m of remediation/resolution plan costs.

Brookfield Infrastructure Partners (BIP) reported fourth quarter and 2014 year-end results, which included quarterly flows from operations (FFO) per unit of $0.86. On a comparable basis, BIP delivered growth of 11% in 2014. The company increased its quarterly distribution to $0.53 per unit, a 10% improvement compared to the prior year. The challenging commodity environment has negatively impacted results at the group's natural gas transmission operations.

Brookfield Property Partners reported strong 2014 fourth quarter and full-year results, including earnings per share of $2.09 for the last quarter and quarterly funds from operations (FFO) per unit of $0.27. The company's board announced a 6% increase in the company's quarterly distributions, from $0.25 to $0.265 per unit.

JPMorgan has agreed to pay $500mn to end more than six years of class action litigation over Bear Stearns' sale of $17.58bn of mortgage securities that proved defective during the U.S. housing and financial crises. The all-cash settlement was made public late Monday, and requires approval by U.S. District Judge Laura Taylor Swain in Manhattan. It resolves claims that Bear, which JPMorgan bought in 2008, misled investors when it sold certificates backed by more than 47,000 largely subprime and low documentation "Alt-A" mortgages in 14 offerings from May 2006 to April 2007....i.e. before JP Morgan bought Bear Stearns.

Royal Bank of Scotland is planning to close at least 99 branches this year despite mounting concern that lenders are leaving communities without access to high street networks. Moray McDonald, a managing director at RBS, said in a Treasury committee meeting on Wednesday that there is a significant shift towards using digital services while branch footfall continues to decline. He said, "We've identified 99 branches we think we would close this year, but I have to say, this is a rolling process for us, so I don't want you to take that as a hard number and the most we would do." Financial Times

Standard Chartered is looking to sell its retail business in the Philippines, part of a wider bid by embattled CEO Peter Sands to cut costs and shrink the bank's asset base, a person with direct knowledge of the matter said. The bank, which entered the Philippines in 1872, would continue to operate its corporate banking business in the country to focus on top clients such as San Miguel, the nation's biggest conglomerate, the source said. Reuters

UBS: According to press reports federal prosecutors in the US have launched a new probe into whether UBS abetted tax evasion by US clients through so-called bearer securities. These securities function essentially like cash, allowing whoever holds the certificate to anonymously claim its value. The reports say that prosecutors in the U.S. attorney's office in Brooklyn are weighing evidence gathered with the FBI as to whether UBS employees either facilitated tax evasion or engaged in securities fraud. UBS paid $780m in 2009 to settle a separate Justice Department tax-evasion probe with the suggestion being these new allegations relate to the period during which UBS was subject to a Non-Prosecution Agreement in relation to that case.

Eurobanks: Collision course on Greece. When two forces drive towards each other, the question is always who will blink first. The risk remains however that neither side do, leading to negative outcomes for both. The ECB's decision to no longer accept Greek government bonds as collateral raises the stakes further on Greek vs Europe negotiations. (i) Greek Central Bank statistics show Central bank lending to Greek banks stood at €56bn at December (up from €45bn in Nov). However, the direct impact may be limited near-term as the Greek Central Bank can continue to provide liquidity to Greek banks through ELA (Emergency Liquidity Assistance) - the opaque structure whereby national central banks can continue to provide liquidity outside the normal ECB collateral limitations, (the sting being that any losses, theoretically, rest with the NCB rather than the Eurosystem). (ii) Use of ELA can itself by limited by a 2/3 majority vote on the ECB council, which itself remains a risk. Inability of the Greek government to bridge finance itself through Tbill issuance bought by the bank sector as planned could limit the time available for a deal to be reached.

Canadian Dividend Payers

BCE Inc Canada's largest telecommunications company, posted a nearly 10% increase in fourth-quarter profit, driven by strong results in its wireless business, and boosted its full-year dividend by 5%. The company also forecast 2015 revenue growth of 1% to 3% and adjusted earnings per share of $3.28 to $3.38, up from $3.18 in 2014. Net income attributable to shareholders rose to $542 million in the quarter from $495 million. On a per-share basis, earnings were flat at $0.64. On an adjusted basis, earnings per share rose to $0.72 from $0.70. Operating revenue rose 2.7% to $5.53 billion. The company added 177,698 net new customers in the fourth quarter for its wireless, television and Internet services.

Global Dividend Payers

ABB – Swiss engineering group took a cautious stance on earnings for the coming months after a strong U.S. dollar, sluggish global economy and a slide in oil prices caused it to miss expectations in the fourth quarter. Like rivals Siemens and Schneider Electric, ABB has been grappling with delayed capital spending by customers that include utility companies and oil, gas and mining businesses. The U.S. dollar has also taken its toll. The currency, in which the Zurich-based company reports financial results, has gained more than 10% against the euro and the Swiss franc over the past year and shaved 6% off ABB's revenues for the fourth quarter. The group said it expects the negative currency effect to persist for the coming quarters, along with increased economic uncertainty, but it declined to provide a forecast for 2015 sales and earnings. On the upside, ABB's reported a 1% rise in orders after currency effects and portfolio changes are excluded and an operating margin increase to 13.3% from 12.5%. ABB sees sales rising by between 4% and 7% to 2020, with core profit margins of 11% to 16%. Fourth-quarter revenue dropped 9% to $10.35 billion. Net profit rose 30% to $680 million, helped by gains from the sale of businesses. ABB said it would raise its 2014 dividend to CHF0.72 per share from CHF0.70 a year earlier.

Emerson – Factory automation equipment maker Emerson Electric Co's quarterly revenue fell slightly due to a strong dollar and divestitures and the company said it now expected sales to fall 1%-4% in 2015. Emerson blamed a strong dollar, lower oil prices and weakness in Europe, Latin America and the Middle East and Africa region for its weak sales forecast. The company sold its power transmission unit in December to Regal Beloit Corp for $1.44 billion, as part of its efforts to focus on its high-growth businesses. Emerson said it would spend $100 million on restructuring in 2015, double the amount it had estimated earlier. The company forecast 2015 earnings of $4.50-$4.60 per share, including a negative impact of a strong dollar, a restructuring charge of $0.05 per share and an estimated gain of $0.75 from divestiture. Emerson's net earnings attributable to common shareholders rose to $525 million, or $0.75 per share, in the first quarter ended Dec. 31 from $462 million, or $0.65 per share, a year earlier. Revenue fell 0.3% to $5.59 billion.

GEA Group – German food processing equipment maker reported a higher-than-expected 11% increase in 2014 adjusted core profit to €591 million, helped by revenue growth and cost cuts. GEA, which derives more than a third of its sales from the dairy industry, expected moderate sales growth and operating EBITDA (earnings before interest, tax, depreciation and amortisation) of €580 to €620 million this year. The company said it would propose increasing its dividend by 17% to €0.70 per share. GEA said 2014 organic or underlying sales rose by 5.6% to €4.52 billion, slightly more than the 5% increase it had signalled last month. Order intake was €4.52 billion, almost flat on a comparable basis.

Syngenta AG the world's largest maker of crop chemicals, has reported an unexpected rise in operating earnings and raised its dividend, as price increases partly offset the effect of declines in the Russian and Ukrainian currencies. Its 2014 margin on core earnings narrowed only slightly to 19.3% from 19.7%. Price increases reduced the hit to earnings from foreign exchange fluctuations to $90 million and helped its 2014 earnings before interest, tax, depreciation and amortization (EBITDA) rise 1% to $2.93 billion, slightly ahead of the expectations. Finance chief John Ramsay told Reuters the company hoped to push through further price increases this year, keeping EBITDA flat from a year earlier. In addition, lower oil prices will mean lower raw material costs, resulting in a positive impact of about $50 million for Syngenta this year and $150 million next year. The recent appreciation of the Swiss franc, following a central bank decision to abandon a cap on the currency, should have a limited impact this year thanks to hedging and would be offset by lower raw material costs next year. Syngenta also said it would pay shareholders a dividend of 11 francs per share, 10% more than a year earlier.

Toyota Motor Corp – lifted its operating profit guidance as a weaker yen increases the value of sales overseas and makes up for slumping demand at home. The yen's decline has been a boon for Toyota, which exports roughly half of its vehicles produced in Japan. Cost-cutting undertaken when the yen hovered at record highs in recent years has also helped the automaker's bottom line. The world's biggest automaker now expects record profit of ¥2.70 trillion ($22.93 billion) for the year ending March 31. That is 8% higher than the previous forecast of ¥2.5 trillion. The revised guidance puts Toyota's operating profit margin forecast at 10.0% from 9.4% based on the previous projection. In the United States, Toyota's biggest market, the automaker has outperformed Japanese rivals thanks to a line-up that spans all vehicle categories. Cheaper fuel has hit sales of the

Prius and other green models but fanned demand for its Lexus luxury brand, pickup trucks and other high-margin vehicles where Japanese peers have fewer offerings. Toyota has a three-year freeze on new factories through March 2016, aimed at preventing unchecked expansion. In the meantime, capacity constraints are widely expected to curb sales growth.

Economic Conditions

US – The non-manufacturing PMI (Purchasing Managers Index), also known as the NMI, a key leading indicator of business activity in the important US services sector, revealed a significantly better outlook than its manufacturing counterpart, according to its latest January reading. The index was up to 56.70 points, ahead of December's 56.50 reading and better than the expected pull-back to a 56.30 points level. The reading was particularly encouraging for the tourism, finance and business support sectors.

The US labour productivity saw a surprising 1.8% drop in the last quarter of 2014, offsetting some of the improvement recorded in the third quarter of the year. Meanwhile, the US trade deficit widened significantly in December, to $46.6 billion against expectations for a $38.0 billion level, as exports retreated by 0.8% and imports advanced by 2.2% on a background of a strengthening US dollar. Imports of energy-related petroleum products advanced by more than 16%, indicating a strong pick-up in demand for oil products as the price of crude tanked around the world.

US employment: U.S. nonfarm payrolls rose a stronger-than-expected 257,000 in January after significantly upwardly-revised gains of 329,000 in December and 423,000 in November. The three-month average of 336,000 is in our view a strong show of confidence, suggesting that companies believe that cheaper fuel will propel the expansion forward despite the strong dollar. Job growth continues to be widespread across industries, with services, manufacturing and construction all posting solid gains, though government pulled back after a spate of hiring. The (more volatile) household survey showed even stronger job growth of 759,000. However, an upward turn in the participation rate (from 37-year lows) drew more than one million people into the labour force, lifting the unemployment a notch to 5.7%. But it's down nearly one percentage point in the past year and still near six-year lows. Average hourly earnings jumped 0.5%, more than retracing a decline the prior month to lift the yearly rate to 2.2%. The latter is still no threat to inflation in our view, but should dispel concerns about possible deflation. In summary, American companies are hiring, and are starting to pay more, too, which should go a long way to sustaining the recent upturn in consumer spending.

Canada – The Canadian balance of trade remained in a deficit for the month of December, to the tune of $650 million, as imports jumped 2.3%, whilst exports only improved by 1.5% in the month. All in a decent result for the Canadian economy, given the drop in energy prices.

Canadian housing starts surprised on the upside in January, reaching an annualized level of 187,300 units, driven by a 12.3% increase in the number of multi-unit starts. Activity was still brisk in the prairie provinces, despite the lower energy price environment, though it is expected to slow down eventually. Activity in Ontario was flat, while British Columbia and Quebec each saw a retreat in their housing starts. The building permits report, released earlier, also revealed stronger than expected housing activity in January, with permits higher by 7.7% in the month, though that improvement came on the heels of a 13.6% drop in the month prior.

Canada employment: stronger-than expected creation of 35k jobs in January pending what is expected to be a difficult patch for the labour market in the next few months. The unemployment rate improved a tenth of a percentage point to 6.6% in January. However, the composition of hiring was titled toward part-time positions (+47k) as full-time employment slipped by 12k. The split across class of worker showed a 41k jump in self-employment while both public (-7k) and private sector (+1k) hiring languished. Across regions, Alberta managed to create 14k jobs despite the national industrial breakdown that showed the loss of 9k positions within extraction. Other industries that showed strength included a 22k jump in professional services and a 11k gain in manufacturing. This latter observation matches some of the encouraging data from the international trade report released yesterday that shows there are some positive growth offsets from the weakness in the energy complex. From the perspective of the Bank of Canada, the soft details of this report when combined with the negative historical revisions announced last week affirm we believe a 'dovish' bias which could mean another 25bps rate cut in March.

Greece - The ECB announced yesterday it would lift its current waiver on Greek Govt Bonds used as collateral by Greek banks for central bank liquidity funding on February 11th. This decision, according to the ECB, is based on the fact that is currently not possible to assume a successful conclusion of the program review and is line with existing Euro system rules. The waiver allowed these instruments to be used in Eurosystem monetary policy operations, despite the fact that they did not fulfill minimum credit rating requirements. Following the announcement, the Greek Minister of Finance stated that by taking this decision the ECB is putting pressure on the Euro group to move quickly on a new mutually beneficial deal between Greece and its partners. The MoF further noted that the ECB's decision will not reflect any concerns about the health of the local banking system, adding that the govt will not change its negotiating strategy. Greek banks will still have access to funds through the Bank of Greece Emergency Liquidity Assistance (ELA). However, ELA costs will be considerably higher and the president of Germany's Bundesbank Jens Weidmann called for a tough stance of the ECB in awarding emergency liquidity assistance. "I feel that we should apply strict standards regarding ELA," Weidmann told business daily Boersen-Zeitung. "Governments and parliaments have to decide whether and how banks should be kept afloat."

The Greek Prime Minister addressed parliament on Sunday outlining his government's pledges for the next four years and seeking a vote of confidence on Tuesday night. In our view he didn't leave much room for compromise with Europe, sticking to his main campaign promises that include a hike in minimum wage, rehiring of un-constitutionally sacked workers in public sector, claw back of several reforms sanctioned by Troika under previous govt (including 13th pension for those below €700/month) and changing existing legislation to allow govt to have full voting rights over banks (based on stakes that are non voting right now). He said he would not ask for extension to existing failed bailout program, but will continue to seek bridge financing till June, something that Europe has already dismissed. Separately, Standard & Poor's lowered its long-term sovereign credit rating for Greece by 1 notch to 'B-' from 'B'. The long- and short-term ratings on Greece remain on CreditWatch with negative implications. S&P notes that the downgrade reflects its view that the liquidity constraints weighing on Greece's banks and its economy have narrowed the timeframe during which the new government can reach an agreement on a financing programme with its official creditors.

Reserve Bank of Australia cut rates 25bps down to 2.25%. The RBA followed the Bank of Canada's example provided very little guidance ahead of the decision with only media analysts warning of a possible cut. The RBA cited international events in its action, likely looking at weak commodity prices, other central bank policies and slower global growth.

Financial Conditions

US Federal Reserve policymakers remain determined to signal that although Quantitative Easing has stopped, the stimulus remains via keeping rates at present low until mid 2015. The US 2 year/10 year treasury spread is now 1.29% and the UK's 2 year/10 year treasury spread is 1.19% - 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 US 30 year mortgage market rate has increased to 3.59% - (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 US housing inventory is at 5.1 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 18.84 (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 6 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

Private/Alternative Products

Portland also currently offers 4 private/alternative products:

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

Net Asset Value:

The Net Asset Values (NAV) of our investment funds are published on our Portland website at http://www.portlandic.com/prices/default.aspx

Sources: Thomson Reuters, Bloomberg, KBW, BMO, Scotiabank, Macquarie, Credit Suisse

Source:Thomson Reuters, Bloomberg, KBW, BMO, Scotiabank, Macquarie, Credit Suisse

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