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Owner Operated Companies

Alphabet Inc.'s Google unveiled the third edition of its Pixel smartphone, a Google Home smart speaker with a display and its first tablet computer as it makes a come-from-behind push into hardware. The Pixel 3, priced at $799, and a larger Pixel 3 XL, priced at $899, mark Google's latest entries for a phone lineup it hopes will someday be as popular as Apple Inc.'s iPhone. The Pixel Slate tablet runs Google's beefier Chrome OS laptop operating system rather than Android. It is priced at $599, aimed at competing with Apple's iPad Pro. A new artificial intelligence tool sure to generate buzz among consumers also could be helpful. The software, launching on U.S. Pixels only, answers calls, requests information about the nature of the calls and shares it as text with the recipient. Google shipped 2.53 million Pixel 2 and 2 XL devices through the nine months ended June 30. The first Pixel devices hit 2.4 million shipments in the nine months ended June 30, 2017, the firm said.

Canopy Growth Corporation announced it had agreed to acquire the assets of hemp research company Ebbu Inc. Canopy is reportedly to pay Ebbu CAD $25 million in cash and issue 6.2 million shares for buying assets, including IP (intellectual property) and research, for its hemp and THC-rich cannabis genetic breeding program and cannabis-infused beverage capabilities. Up to CAD $100 million more in purchase price will be payable if certain scientific related milestones are achieved within two years following closing, with the deal expected to close in Nov. 2018. "By applying Ebbu's IP, the company has the potential to vastly reduce the cost of CBD production, a sought-after cannabinoid in both the wellness and medical spaces", according to Canopy.

Fortis Inc. has released its five-year capital investment plan of $17.3 billion for the period 2019 to 2023, up $2.8 billion from the prior year's plan. Consolidated rate base is projected to increase from $26.1 billion in 2018 to approximately $32.0 billion in 2021 and $35.5 billion in 2023, translating into a 3 and 5-year compound annual growth rate of 7.1% and 6.3%, respectively. The corporation's board of directors also announced a $0.025 or 5.9% increase in the fourth quarter 2018 common share dividend. "Key industry trends, including grid modernization, the delivery of cleaner energy and electrification, will result in incremental investments in the U.S. Midwest ($900 million), Arizona ($600 million) and Ontario ($600 million)," said Barry Perry, CEO. Beyond the base capital investment plan, Fortis continues to pursue additional sustainable organic growth and near and long-term development projects. Key development projects not yet included in the capital investment plan include a small-scale LNG (liquid natural gas) export terminal at the Tilbury facility in British Columbia; the fully permitted, cross-border Lake Erie connector electric transmission project in Ontario; and the Big Chino Valley pumped storage project in Arizona. Marking its 45th consecutive year of increased dividends, the board declared a common share dividend of $0.45 per share. In addition, the corporation has targeted average annual dividend per common share growth of approximately 6% through 2023 based on an annualized dividend of $1.70.

Walgreens Boots Alliance, Inc. reported results for the last quarter of its 2018 fiscal year, including revenue which rose nearly 11% to $33.44 billion, just short of the average analyst estimate of $33.78 billion, according to I/B/E/S data from Refinitiv. The company's quarterly profit, however, beat analysts' expectations, helped by its purchase of rival Rite Aid Corporation stores. "Our businesses have mostly done a good job of growing or at least holding their own in a tough year in many of our markets," CEO Stefano Pessina said. Walgreens forecast 2019 adjusted profit of $6.40 to $6.70 per share, compared with the average analyst estimate of $6.45 per share, although it said that number included the effect of $3 billion of share repurchases this year. Excluding items, the company earned $1.48 per share, beating analysts' expectation of $1.45 per share. Same-store sales at its pharmacies rose 1.3%, beating analysts' expectations for a 0.57% rise.

Energy Sector

Nothing significant to report.

Financial Sector

Bank of America Corporation reported Q3 2018 EPS of $0.66. Consensus was $0.62. Results benefited from a $216 million loan loss reserve release ($0.02), as well as a gain on sale of an equity investment (Global Markets) and a small gain from the sale of non-core consumer real estate loans, neither of which was quantified in the release. It also recorded a $99 million Debt Value Add adjustment (cost it $0.01). Relative to consensus, its loan loss provision and tax rate were lower than expected, while fee income was higher than anticipated, though the gains helped. Net interest income (NIM better than expected, loans worse) and expenses approximated expectations. Operating revenues increased 4% year/year but were little changed linked quarter at $22.7 billion. Tangible book value increased 0.9% to $17.23 (1.7x). It posted a ROE of 10.99%. Its CET 1 ratio was 11.4% and its Risk Weighted Assets declined 0.3%. Average diluted shares declined by 1.4%.

Citigroup Inc. reported Q3 2018 EPS of $1.73. Consensus was $1.69. Results included a $250 million ($0.08) gain on the sale of an asset management business in Mexico. It also had a $150 million release build (a $186 million build in Global Corporate Banking and $7 million build in Institutional Corporate Group, as well as a $43 million release in corporate/other). We believe Citi remains on track to achieve roughly 100bps of efficiency improvement this year, putting its 2018 efficiency cost / income ratio in the 57.3% area. Citi believes it has reached an inflection point where its efficiency savings should start outpacing incremental investment spend. This dynamic should become clearer in 2019. In addition, 2019 should benefit from higher reported revenue growth in its branded card business given to higher interest-earning loan growth and a decline in promotional rate balances.

HSBC Holdings PLC has finalized a $765 million settlement over the sale of mortgage-backed securities in the run-up to the financial crisis. The U.S. Department of Justice announced the civil penalty on Tuesday, which draws a line under claims that the bank misled investors about the quality of loans it packaged up into securities from 2005 to 2007. Bob Troyer, the U.S. Attorney for the District of Colorado, said HSBC had made "made choices that hurt people and abused their trust". "HSBC chose to use a due diligence process it knew from the start didn't work. It chose to put lots of defective mortgages into its deals. When HSBC saw problems, it chose to rush those deals out the door," he said in a statement announcing the settlement. (Source: Financial Times)

JPMorgan Chase & Co. reported Q3 2018 EPS of $2.34, better than consensus of $2.26. This is the 15th consecutive quarter JPMorgan has exceeded consensus. Core EPS looks to be around $0.07 higher. Higher than expected fee income and a lower than anticipated loan loss provision drove the upside. Trading results were a little better than its September forecast. Its 2018 'Outlook' lowered its 2018 credit card loss guidance to 3.10% from the previous range of 3.25-3.50%. It posted a ROTE of 17%, CET 1 ratio of 12.0%, an overhead cost / income ratio (adjusted) of 56%.

Activist Influenced Companies

Pershing Square Holdings, Ltd. – Bill Ackman said that his activist hedge fund Pershing Square Capital Management, L.P. has built a roughly $900 million position in Starbucks Corporation, betting the world's biggest coffee chain can overcome stagnant sales in its home market. Ackman's unveiling of a 1.1% stake in Starbucks comes as the Seattle-based company is trying to convince investors it can fend off heavy competition from rivals, including fast-food chains and high-end coffee shops. Last month, it announced a reorganization that includes leadership changes and job losses. While activist shareholders are known to pick fights with chief executives and corporate boards, Ackman sounded a conciliatory tone as he unveiled Pershing Square's investment at the Grant's Fall 2018 Conference in New York. Ackman said recent actions by Kevin Johnson, who took over from Howard Schultz as Starbucks CEO last year, were "encouraging" and that Starbucks' recent challenges are "fixable with appropriate management execution." Schultz stepped down as Starbucks' executive chairman in June. Ackman praised the re-evaluation of Starbucks' portfolio, the closure of Teavana stores, a rejiggering of its owned and licensed businesses, its cost-cutting initiatives and a $19 billion three-year share buyback program. In his presentation dubbed "Doppio" - a reference to a double shot of espresso - Ackman said Starbucks' share price could more than double over the next three years if the company can meet its targets. After three years of losses at Pershing Square, Ackman has adopted a lower profile that appears to be paying off, with his hedge fund up 13.8% in the first nine months of the year. The average hedge fund has gained less than 2% during the same period. This is partly thanks to Ackman's managing to turn previous losses into wins. Last year, he lost a bitter proxy contest against payroll processing company Automatic Data Processing Inc., yet the company's recent strong performance has boosted his portfolio. Pershing Square, which has $8.4 billion in assets under management, has also unveiled positions this year in Nike Inc., United Technologies Corporation and Lowe's Companies, Inc. None of these investments resulted in a public fight, and Pershing Square has already exited Nike. Historically only one or two of Ackman's roughly one dozen positions develop into the kind of public fights that make headlines, like the short bet against Herbalife Nutrition Ltd. or his effort to rescue drug maker Valeant Pharmaceuticals International, Inc. that cost him billions of dollars. Ackman also has experience in the food retail sector, having invested in McDonald's Corp over 10 years ago and in Chipotle Mexican Grill Inc. more recently.

Dividend Payers

AT&T Inc. is reportedly preparing to launch a subscription video service by the end of 2019 that will offer movies and TV shows from Hollywood's biggest library, as well as licensed programming from other companies and, within a year, original content. The service, to be anchored by HBO, will include everything from film classics like "Casablanca" to the "Harry Potter" and "Batman" franchises to TV series "ER" and "Pretty Little Liars." The announcement of the service delivers on a promise AT&T made in June after shareholders approved the telecom company's $85 billion purchase of Time Warner Inc. in order to make more money selling products directly to consumers rather than just go through middlemen such as cable companies.

Barrick Gold Corporation announced preliminary Q3 production of 1.15 million ounces (Moz), up from Q2 2018 production of 1.07 Moz (+8%) and broadly in line with guidance of 1.2 Moz. Production has increased as operations have recovered at Porgera following earlier earthquake damage and scheduled maintenance downtime at both Pueblo Viejo and Barrick Nevada earlier this year. Gold sales were broadly in-line with estimates, driven by an inventory release at Barrick Nevada (51K ounces) and Porgera (9K ounces). Barrick expects cash costs to be 1-3% lower relative to Q2 2018 ($605/oz) and 7-9% lower on all-in sustaining costs (Q2 2018 of $856/oz). Copper production was 106 million pounds (Mlb), up 28% from the prior quarter (83Mlb) and slightly below estimates of 109Mlb. Copper sales were 114Mlb. Barrick expects Q2 copper cash costs to be 7-9% lower (Q2 actual $2.10/lb), driven by improved grade, recovery and crusher reliability at Lumwana. Barrick maintained its 2018 gold production guidance of 4.5-5.0 Mozs and noted that it expects gold production of 1.25Moz in Q4, implying 2018 production of 4.52Moz.

GEA Group AG pre-announced Q3 2018 results slightly ahead of expectations and consensus but made changes to fiscal year (FY) 2018 guidance. Bottom line is that the new FY 2018 EBITDA guidance of €540 million is only -2% below consensus (which was already below GEA's old guidance). The specific new guidance for FY 2018 sales growth (excluding foreign exchange (FX) but including 4% from mergers & acquisitions) is raised to 7.5% (previously 5-6%) but EBITDA margin expectations were lowered to 11.1% in constant currency or 11.3% reported including FX (previous guidance of the lower end of 12%-13% in constant currency). To put this margin discussion further into context GEA's mid-term margin group margin target is 13.5%-15.5%. We believe due to GEA's depressed end markets (Dairy) it has scope to recover, and like its defensive / under-utilized balance sheet but keenly await the new CEO to take a more active approach to the portfolio of assets.

Economic Conditions

U.S. consumer prices rose just 0.1% in September, below expectations for a 0.2% rise, and is now up 2.3% above a year ago. The two most volatile items food and energy… were pretty tame. Food was unchanged, and energy was down 0.5%. Excluding food & energy, prices were also up just 0.1%, missing expectations, and are 2.2% above year-earlier levels. There was likely a tariff-effect playing out in the apparel department as clothing costs jumped 0.9%. This was the biggest increase since February and follows three consecutive monthly declines. The strong U.S. dollar likely had a role in keeping prices from rising more. New car prices were down 0.1%, the first decline since February despite higher costs for steel. And, medical care costs edged up 0.2%, the first increase in three months.

U.S. retail sales have disappointed for two months in a row. Last month, huge upward revisions for the August release provided a big offset. Today's report for September, however, did not have that to fall back on. In fact, there were small downward revisions to the prior two months. Total retail sales were unexpected soft, rising just 0.1% in September, the second monthly gain of that size. Autos and parts were up 0.8% with sizeable gains in sales of furniture, electronics, clothing and sporting goods continuing to point to a confident consumer.

The International Monetary Fund said the world economy is plateauing as the lender cut its growth forecast for the first time in more than two years, blaming escalating trade tensions and stresses in emerging markets. On the eve of its annual meetings in Bali, Indonesia, the fund last Tuesday projected a global expansion of 3.7% this year and next, down from the 3.9% projected three months ago. It was the first downgrade since July 2016. While the global economy is still on track to match last year's pace, which was the strongest since 2011, the new outlook suggests fatigue is setting in and the overall performance masked mounting weakness in emerging markets from Brazil to Turkey. (Source: Bloomberg).

The International Monetary Fund (IMF) has warned a trade war between the U.S. and China risks making the world a "poorer and more dangerous place" in its latest assessment of the global economy. The IMF has lowered its forecast for global growth this year and next. It said that a full-blown trade war between the U.S. and China would put a significant dent in economic recovery. Its chief economist said further trade barriers would hit households, businesses and the wider economy. "Trade policy reflects politics and politics remain unsettled in several countries, posing further risks," said Maurice Obstfeld (Source: BBC).

Financial Conditions

The Globe & Mail reported last week that notoriously indebted Canadian households are finally addressing their financial health, but while this is a positive for the economy's long-term outlook, it will not be without economic pain that is already visible in cratering auto-sales data. The clearest sign of improvement in domestic household balance sheets is the significant change in trend for the ratio of debt to disposable income. Until recently, the post-financial crisis time period has seen Canadian consumer debt rise considerably faster than income. Between March 2009, and December 2016, household debt went from 150% of disposable income to 172%. Canadians, however, appear to have started addressing their debt situation as 2017 began. The steep drop in the blue line indicates that the pace of debt accumulation slowed dramatically relative to income growth. It is likely not coincidental that the pace of housing-value appreciation began to drop six months later. As it stands, the annual rate of change in debt to disposable income has been negative since the beginning of this year – income is now growing faster than debt for the first time in over a decade. Canadian retail spending and overall gross domestic product (GDP) growth are also slowing along with the improvement in debt to disposable income ratios. There is nothing dire in recent results, but it's still notable that annual retail spending growth slowed from 7.3% to 3.7% in the first six months of 2018. GDP growth dropped from 4.1% to 2.4% in the same time frame.

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The trend in which household-debt deleveraging crimps growth in real estate prices, consumption and GDP growth could continue for a long time. Despite recent improvement, the debt to disposable income ratio remains elevated at 171%, well above the 20-year average of 142.4%. National growth is likely to disappoint as long as the household debt situation is being addressed.

The U.S. 2 year/10 year treasury spread is now 0.30% and the U.K.'s 2 year/10 year treasury spread is 0.79% - 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 two-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 4.90% (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 4.0 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 21.64 (compares to a post-recession low of 9.52 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.

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 and McKinley Funds
- 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) 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.

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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, 'ROE' return on equity, 'ROTE' return on common equity.

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