

DM Monthly Report

OCTOBER 2017

PORTFOLIO ACTIVITY

Aside from rebalancing transactions, no positions were added to or sold from DM mandates during September.

FEATURE STOCK

Oracle Corp. (ORCL)

Several years ago, ORCL embarked on a significant business transition which would see the company embrace the emerging “cloud” segment of its industry. The shift from a traditional licensing model to a ‘software-as-a-service’ (or SaaS) approach has been a herculean undertaking but is now paying off, both through recent earnings generation and in the company’s positioning for future growth. In ORCL’s most recent quarterly update, it reported cloud revenue growth of 51% and said that it would hire another 5000 engineers, consultants, and salespeople to support the department. Bolstered by this momentum, CEO Mark Hurd referenced the competition, noting that ORCL’s cloud apps business was growing more than twice as fast as that of Salesforce.com and that the company has 30 times as many ERP (enterprise resource planning) customers as Workday. Despite softness in the stock following its September earnings release—which we used as an opportunity to boost our position—ORCL has returned more than 28% for our portfolios in 2017.

WHAT WILL IT TAKE TO JUMPSTART THE TSX?

In our third quarter portfolio commentary, we highlighted the recent contrast between the Canadian economy, which has led all G7 countries in growth for each of the past four quarters, and the TSX, which is the worst performing stock market amongst that same group so far this year. On the bright side, lethargic Canadian share prices combined with rising earnings have pushed the relative valuation of the TSX down to multi-year lows against the S&P 500; unfortunately, though, it’s hard to know when global capital will start to take notice of this comparative advantage and begin to shift back to our market.

Aside from the valuation story, a clue to what could put Canada back in vogue may be found in the constitution of our market. As the blue bars in the busy chart below indicate, no major index has as much exposure to financial services and energy as does the TSX and, by extension, no one else is as positively tilted toward rising interest rates and higher oil and gas prices. For the moment at least, rates are on the climb, meaning that our lifecos should see some relief in the pricing of their future liabilities and banks may begin to gain breathing room in the spread they earn between deposits and loans. But what about energy?

To be sure, this is perhaps the least popular market sector at the moment, with downbeat public opinion and political ambivalence (at best) only compounding concerns around commodity pricing and new sources of supply. These same forces, however, have notably curtailed industry investment, with funds deployed to securing future production markedly down from typical levels. At the same time, possible new sanctions against Iran and Venezuela, along with unrest in Kurdistan, raise the prospect of a geopolitical supply interruption. On the other side of the equation, global demand for crude continues to rise, even in the face of the prevalent “death of oil” narrative and the idea that the internal combustion engine is living on borrowed time. Against this supply/demand backdrop, the investment case for energy—and for Canada—could reverse itself quickly.

