

PALOS

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Weekly Commentary

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By Charles Marleau CIM[®] and William Mitchell CIM[®]

In the Oil Patch, it's About Returning Cash to Shareholders

The world's five largest oil producing companies are located outside of North America: Saudi Aramco (#1-Saudi Arabia), Rosneft (#2-Russia), Kuwait Petroleum Company (#3-Kuwait), The National Iranian Oil Company (#4-Iran) and The China National Petroleum (#5-China). These companies produce an estimated 3 million to 10 million barrels of oil equivalent per day (boe/d). By contrast, the largest companies by production in the U.S. are **ExxonMobil Corp (XOM:NYSE)** at about 3.8 million boe/d (Q4/2022) and **Chevron Corp (CVX:NYSE)** at 3.0 million boe/d of global production (2022). **Suncor Energy (SU:TSX/NYSE)** is Canada's largest producer exceeding 700 thousand boe/d (Q4/2022).

Chevron reported full-year 2022 earnings on January 27. In a press release, Chairman and CEO Mike Wirth stated that the company delivered "record earnings and cash flow in 2022 while increasing investments and growing U.S. production to a company record". Adjusted EPS (earnings per share) was US\$18.83 per share-diluted for 2022 versus US\$8.14 per share-diluted in 2021. The company hiked its dividend by 6 percent marking the thirty-sixth straight year of increases. Additional cash was returned to shareholders via "buybacks", an exercise where a company's management authorizes share repurchases on the stock exchanges. In theory, a reduction in shares increases the value of shares held. The repurchase rate in 2022 was US\$15 billion and management announced that it has approved an additional US\$75 billion in buybacks.

Exxon reported on January 31. Full-year earnings were US\$55.7 billion compared with US\$23.0 billion in 2021; a 242% increase. Cash redistributed to shareholders totaled US\$29.8 billion with half coming in the form of dividends and the other half from repurchases. Management announced an additional US\$35 billion in repurchases for 2023-2024. Impairments from the divestment of its Russian assets and rising inflation were offset by favourable pricing, capital discipline and record North American refining throughput. Debt retirements totaled US\$7.2 billion in 2022 and cash-on-hand of US\$29.7 billion "further strengthened the balance sheet" and offers greater "financial flexibility" moving forward.

During last Tuesday's State of the Union address, President Biden remarked that the United States will need oil "for at least another decade". These comments were apparently unscripted and caught many people off

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guard. Biden's comments seemingly conflict with his climate change agenda which aims to curtail oil dependence and cut emissions by 50 percent by 2023 and achieve net zero by 2050. While reducing global carbon emissions is crucial to winning the battle against global warming, the fact remains that the world will continue to consume oil as the clean energy transition progresses. This is simply a fact-based truth.

Canada's major oil companies began reporting on January 31 with Calgary based **Imperial Oil (IMO:TSX/NYSE)**. Financial results were "the strongest in company history" according to President and CEO Brad Corson. IMO returned over \$7 billion to shareholders in 2022 through dividends, share buybacks and a \$1.5 billion substantial issuer bid (SIB) in December. An SIB is a mechanism that's used to distribute excess cash to shareholders via a publicly announced auction in which shareholders may elect to tender shares. Upon completion, IMO's SIB, which was oversubscribed, resulted in 3.4% of IMO's outstanding shares being repurchased and cancelled. ExxonMobil, Imperial's majority shareholder, tendered proportionally to maintain its 69.6% ownership stake.

In our view, Canada is home to the most responsible oil companies in the world and this is why we focus our attention on Canadian producers. In virtually all instances, boardrooms across the country have implemented policies addressing and enshrining environmental, social, and governance (ESG) policies as standard business practice. The **Pathways Alliance** is a carbon reduction initiative between Canada's six largest oil sands companies and includes CNQ, CVE, IMO, SU, MEG Energy, and ConocoPhillips Canada. These companies account for 95% of oils sands production. The alliance plans to achieve net zero greenhouse gas emissions by 2050.

Canada's oil patch acknowledges the need for a sustainable energy future and, further, understands the need to work with governments, industry participants, indigenous communities, and stakeholders. Plans to decarbonize are ambitious and participants agree that there is no "single path" to net zero. What's understood is that innovations like carbon capture and storage (CCS), clean hydrogen, and renewables, will require fiscal and regulatory assistance from governments. For CCS, new infrastructure will be needed to transport CO2 from the oil sands to underground storage sites. Incentives to transition to renewables would also go a long way.

This week we anticipate earnings from two of Canada's other largest producers: Suncor Energy on Tuesday and **Cenovus Energy (CVE:TSX/NYSE)** on Thursday. Canada's most senior energy company by market cap, **Canadian Natural Resources (CNQ:TSX/NYSE)**, will report on March 2. We will be monitoring these events closely and be on the earnings calls with management which customarily follow an earnings release. We expect that the remarkable turnaround in Canada's oil patch, which occurred in a relatively short period of time, is set to continue. Investors in the oil sector surely recall the dark days of "diminishing reserves" and widespread calls for "an end to oil". We believe the trend of returning cash to shareholders will persist and investors who stay the course will continue to be rewarded for their patience.

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Save for your future by contributing to a Registered Retirement Savings Plan (RRSP)

RRSP Benefits:

- RRSP contributions are a good way to reduce your taxable income
- Your investments grow tax deferred while held in your RRSP
- When you retire you can use your RRSP to receive regular income
- A spousal RRSP can reduce your combined tax burden
- You can borrow from your RRSP to buy your first home or pay for your education

RRSP Contribution Details:

- The **deadline** for making your 2022 RRSP contribution is March 1, 2023.
- Your **2022 RRSP contribution limit** is calculated as 18% of your 2022 earned income up to a maximum of \$29,210. The maximum will increase to \$30,780 in 2023.
- If you've already made your 2022 RRSP contribution, consider making your 2023 contribution in January 2023 to benefit from the power of tax-deferred growth.
- Unused contributions can be carried forward from a previous year. You can find your RRSP contribution information on your most recent CRA **Notice of Assessment**, or by calling the **CRA Tax Information Phone Service (TIPS)** at 1-800-267-6999.

The sooner you start contributing to an RRSP or TFSA, the more time you'll have to grow your money until it's time to retire. There's nothing like the power of tax-free compounding returns.

If you would like to open an RRSP account, contribute to an existing or Spousal RRSP, or if you have any questions about RRSPs, please contact your Palos Advisor.

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Save for your future by contributing to a Tax Free Savings Account (TFSA)

TFSA Benefits:

- TFSA investments grow tax free (Interest, capital gains and dividends are tax exempt)
- Withdrawals can be made whenever you wish and unlike an RRSP, they are tax-free
- TFSA contribution limits are not reduced following a withdrawal
- Withdrawals can be re-contributed in a subsequent calendar year(s)

TFSA Contribution Details:

- The TFSA contribution limit for 2022 is \$6,000 and will increase to \$6,500 in 2023
- TFSA contribution limits are cumulative since TFSA's were introduced in 2009. If you were born after 1991, your lifetime contribution limit including 2023 is \$88,000
- Canadian residents 19 years of age and who have a Social Insurance Number are eligible to open a TFSA
- To determine your TFSA contribution limits, you can refer to your most recent CRA **Notice of Assessment**, or by calling the **CRA Tax Information Phone Service (TIPS)** at 1-800-267-6999

TFSA's are an excellent way to save for your future

TFSA's can complement your taxable retirement income from a taxable account (RRSP, RRIF, LIRA)

The sooner you start contributing to TFSA, the more time you'll have to grow your money.

If you would like to make a TFSA contribution or open an TFSA account, please contact your Palos Advisor.

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Épargnez pour votre avenir en cotisant à un régime enregistré d'épargne-retraite (RÉER)

Les avantages d'un RÉER:

- Les cotisations à un REER sont un bon moyen de réduire votre revenu imposable.
- Vos placements bénéficient d'un report d'impôt lorsqu'ils sont détenus dans votre RÉER.
- Lorsque vous prenez votre retraite, vous pouvez utiliser votre RÉER pour recevoir un revenu régulier.
- Un RÉER de conjoint peut réduire votre charge fiscale combinée.
- Vous pouvez emprunter de votre RÉER afin d'acheter votre première résidence ou pour financer des études.

Les choses à savoir :

- **La date limite** de cotisation au RÉER pour 2022 est le 1er mars 2023.
- Votre **plafond de cotisation au RÉER pour 2022** est calculé à partir de 18% de vos revenus gagnés en 2022, jusqu'à un maximum de 29 210 \$. Ce maximum sera augmenté à 30 780 \$ en 2023.
- Si vous avez déjà cotisé à votre RÉER pour 2022, envisagez d'effectuer votre cotisation de 2023 en janvier 2023 afin de bénéficier dès maintenant de l'effet différé des impôts.
- Les cotisations non-utilisées peuvent être reportées d'une année précédente. Vous pouvez vous renseigner sur vos cotisations à un RÉER en consultant votre **avis de cotisation le plus récent de l'ARC** ou en appelant **le Système électronique de renseignements par téléphone (SERT)** au 1-800-267-6999.

Le plus tôt vous commencerez à cotiser à un RÉER ou à un CELI, le plus longtemps vous disposerez pour faire fructifier votre argent jusqu'au moment de la retraite. Rien ne vaut la puissance des rendements composés non imposables.

Si vous souhaitez ouvrir un compte RÉER, contribuer à un RÉER existant ou à un RÉER de conjoint, ou si vous avez des questions sur les RÉER, veuillez communiquer avec votre conseiller Palos.

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Épargnez pour votre avenir en cotisant à un compte d'épargne libre d'impôt (CELI)

Les avantages du CELI:

- Faire fructifier votre épargne à l'abri de l'impôt (les intérêts, les gains en capital et les dividendes seront non taxables)
- Vous pouvez effectuer des retraits quand vous le désirez et contrairement à un REER, ils ne seront pas taxables.
- Vos limites de contribution à un CELI ne seront pas réduites à la suite d'un retrait de celui-ci.
- Vos retraits peuvent être de nouveau cotiser dans les années subséquentes.

Les choses à savoir :

- Le montant limite de cotisation à un CELI pour 2023 est de \$6,500
- Depuis leur introduction en 2009, les limites de contributions à un CELI sont cumulatives. Si vous êtes nés après 1991, votre limite de contribution à vie est de \$88,000 (2023 compris) .
- Si vous êtes un résident canadien de plus de 19 ans et que vous détenez un N.A.S. Vous êtes alors éligible à un CELI.
- Si vous voulez connaître vos limites de contribution, vous trouverez toutes les informations pertinentes sur votre plus récent **avis de l'ARC**. Vous pouvez obtenir également ces renseignements par l'entremise du **Système électronique de renseignements par téléphone (SERT)** en composant le 1-800-267-6999.

Le CELI est un excellent moyen d'épargner pour votre avenir

LE CELI est un appoint de revenu qui vient compenser les montants qui sortiront des régimes enregistrés et qui eux sont imposables (REER, FERR & CRI)

Le plus tôt vous commencerez à faire des contributions à votre CELI, plus vous aurez du temps devant vous pour faire fructifier votre épargne.

Si vous souhaitez ouvrir un compte CELI ou faire une cotisation à votre CELI, veuillez contacter votre conseiller à Palos.

Chart 1: Palos Domestic Funds versus Benchmarks (Total Returns) ¹	FundServ	NAVPS	YTD Returns
Palos Income Fund L.P.	PAL100	\$8.84	7.17%
Palos Equity Income Fund - RRSP	PAL101	\$6.90	6.08%
Palos WP Growth Fund - RRSP	PAL213	\$13.78	10.43%
Palos-Mitchell Alpha Fund ³	PAL300	\$9.36	17.41%
S&P TSX Composite (Total Return with dividends reinvested)			6.62%
S&P 500 (Total Return with dividends reinvested)			6.70%
S&P TSX Venture (Total Return with dividends reinvested)			7.58%
Chart 2: Market Data ¹			Value
US Government 10-Year			3.73%
Canadian Government 10-Year			3.15%
Crude Oil Spot			US \$79.72
Gold Spot			US \$1,862.80
US Gov't 10-Year/Moody BAA Corp. Spread			185 bps
USD/CAD Exchange Rate Spot			US \$0.7494

¹ Period ending February 10th, 2023. Data extracted from Bloomberg

² Fund is priced annually

³ Fund is priced weekly on Tuesdays

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