Canada offers solution to Europe’s energy problem, says bullish Middlefield

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By **Jamie Colvin** / 06 Apr, 2022

Following the war in Ukraine, Europe will ditch Russia as its oil supplier and turn to energy-abundant Canada, predicts Dean Orrico, fund manager of **Middlefield Canadian Income Trust** (MCT).

Skyrocketing oil and gas prices and concern over energy security after Russia invaded Ukraine have forced many national leaders to find a more stable source to bridge the transition to green energy. Resource-rich Canada offers a solution, Orrico told Citywire.

Canada is the world’s fourth-largest oil producer, according to Bloomberg, and provides a more secure source of energy for Europe while it builds liquefied natural gas (LNG) export terminals to ship natural gas, Orrico said.

‘Europe became reliant on Russia for oil and natural gas and I don’t think we’re ever going back to the point where Russia will be supplying 40% of Europe’s natural gas needs.’

The £144m investment company which he manages with Robert Lauzon at Middlefield Group in Toronto, has a ‘value’-oriented portfolio, with financials, energy and property each making up about 30% of assets.

It’s benefited from the global stock market swing from ‘growth’ to value and the surge in commodities with the shares rallying 21% in the past month, taking its one-year advance to 40.4%.

As London’s only listed Canadian fund, the trust has delivered a 70.5% total return to shareholders over three years, giving US-focused rivals a run for their money, although behind **JPMorgan American** (JAM) and **Baillie Gifford US Growth** (USA) which have returned 83% and 95%, according to Numis Securities data.

The Jersey-based but London-listed closed-end fund invests 94% in Canada with the rest in the US. It includes oil and gas companies as well as oil pipeline companies, Enbridge and Pembina, as Orrico bullishly bets on prices staying relatively high in Canada for the foreseeable future.

'Utility-like' pipelines have predictable cash flows, but also have an overriding ability which allows them to benefit from higher oil and gas prices. High demand has led to payout yields between 5% and 7%, he said.

Pipelines operate on a take-or-pay system, which means oil and gas companies rent the pipeline to transport an agreed volume of oil to a refinery, for example.

Shares in 5.3%-yielding Pembina have risen 22% this year with 6%-yielding Enbridge up 17%.

'It's making even more of a case to invest in Canada, which is a very stable country with an abundance of resources, a stable economy and provides security of energy supply,' Orrico said.

He pointed to oil and gas producer **Canadian Natural Resources**, which he bought in 2019, as an example of a high-performing holding. The 3.9%-yielding shares have nearly doubled in the past year to become the trust's biggest holding at the end of February accounting for 5.5% of assets.

Last month the company reported a rebound in its fortunes after the disruption of the pandemic with 2021 profits jumping to C$7.66bn on $30.1bn of revenues from a loss of $435m on $16.9bn in 2020. Dividends grew 28%.

Trimming gearing, or borrowing, from about 21% to 19% in March, Orrico said he had not been this bullish about Canada in years, with MCT offering a cheap way of gaining exposure with its shares trading 12% below net asset value. That is slightly narrower than the one-year average discount of 13.7%.

Interest rates in Canada were hiked up to 0.5% last week and inflation rates have stuck at about 5%, but Orrico remains bullish because high rates boost property and financials' performance.

Financials benefit from the higher cost of lending and property from the renegotiations of rent each year in line with the higher rates.

Canada is anticipating over 400, 000 immigrants this year, including many Ukrainian refugees, which will bolster real estate performance as they seek rental accommodation.

'Typically what happens is that during a period of high rates is typically when an economy is growing so you're able to renew your leases at higher levels, more than offsetting the increased cost of your business or the increased interest cost on your debt,' Orrico said.

Orrico has been selling off tech and directing it back into energy, property and financials. American semi-conductor manufacturer BroadCom is the sole remaining tech holding.