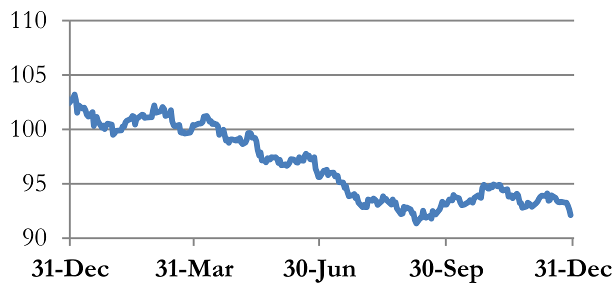
Seamans Capital Management – Q4 2017 Quarterly Report

GLOBAL BONDS AND CURRENCIES

In December, President Trump approved and signed a tax reform bill, thereby taking action on one of his key goals and campaign promises for his first year in office. The bill is expected to have a positive impact on the economy and stock prices in the year ahead.

U.S. Dollar Index



Source: Bloomberg

The U.S. dollar weakened throughout 2017 compared to other global currencies, as seen in the chart above. The government appears to be pursuing a weak dollar policy to improve the global competitiveness of the domestic export economy. Traditionally, the U.S. dollar has been viewed as a "safe haven asset" because the U.S. has never defaulted. This is not important now, with volatility near record lows and investor sentiment favoring risk, causing capital to flow into higher-risk debt and emerging markets. A weaker dollar and lower taxes have left companies in a strong position to post higher earnings.

The Federal Reserve continued raising rates and signaled three more rate hikes in 2018. Fed chairperson Janet Yellen also prepared to step down from her post in the 4th quarter, as Jerome Powell was nominated to replace her. Powell is expected to maintain the same path his predecessor followed, gradually scaling back monetary easing while remaining careful to not create any shocks for the U.S. economy or market. The U.S. market looked favorably on this change, continuing to provide strong returns with low volatility.

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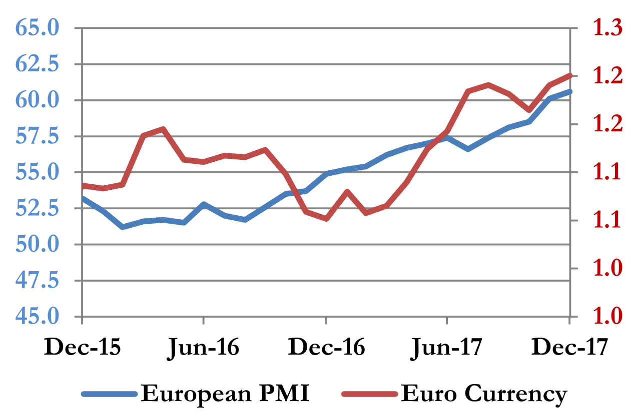
The European manufacturing economy performed well throughout 2017, benefiting from a favorable negotiating position against the UK. The chart below shows that the European PMI, which is a measure of production strength, reached a 17-year high of 60.6; this achievement also helped strengthen the euro. The Catalan independence vote and Merkel's challenge in forging a new government were not serious issues. Lower U.S. corporate taxes, however, have put Europe at a significant competitive disadvantage. This challenge comes at a time when European governments need to raise taxes, immigrants are creating wage deflation, and anti-EU sentiment is rising. While the euro may rise in the first part of 2018, we expect it to decline later in the year.

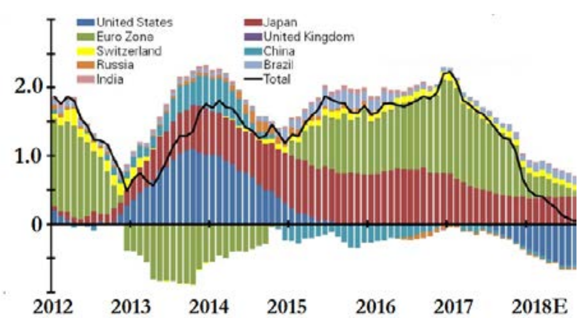
European PMI vs. Euro Price



Source: Bloomberg

The U.S. Treasury yield curve flattened in 2017 as short-term interest rates rose while long-term interest rates fell. Looking forward, we expect that both short- and long-term interest rates will rise by 1% to 1.5% in 2018. Central banks, which have been buying bonds to support the market since 2008, are gradually curtailing their purchases; by June 2018, they are expected to be net sellers, as shown in the chart below. This will be particularly important for Europe because its outstanding sovereign debt rose from 103% of GDP in 2000 to 179% at the end of 2016. We expect interest rates to rise by 2% to 3% to 2008 levels over the next two years.

Central Bank Bond Buying/Selling



Source: Deutsche Bank, Datastream

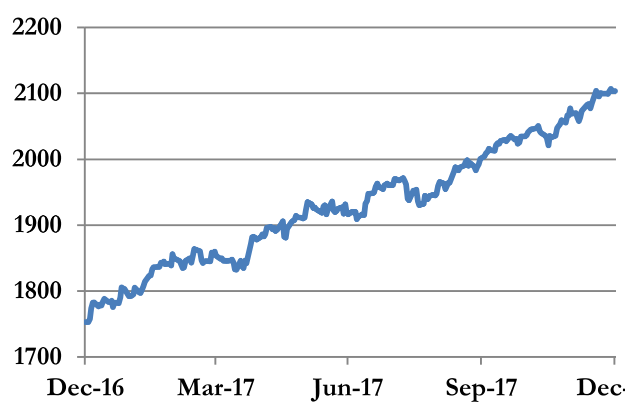
GLOBAL STOCKS

Last year proved to be remarkable not only for the strength seen across markets, but also for the muted volatility. It was perhaps one of the most unloved rallies, as investors generally fought the rising tide. A number of prominent hedge funds were forced to unwind their losing short positions, a process that contributed to the lack of volatility and the slow and relentless rise in stock prices.

The recently enacted tax reform legislation lowers the corporate tax rate from 35% to 21% at the federal level; state and local taxes remain unchanged at about 4%. Tax reform is expected to lead to income gains of 10% to 12% for many U.S. companies. Tax reform also allows companies to repatriate the trillions of dollars that they hold offshore at a 15.5% rate for liquid assets and 8% for illiquid assets.

In January 2018, Apple announced that it would repatriate $245 billion and pay $38 billion in U.S. taxes. In addition, the company said that it will be giving employees a one-time $2,500 bonus, make $30 billion in capital expenditures, and create 20,000 jobs over the next five years. Apple represents a small portion of the estimated $4 trillion in cash held by U.S. companies abroad. Other companies are expected to use repatriated funds for mergers and acquisitions, share buybacks and dividend increases. All of these initiatives will support further gains in the stock market over the next few years.

MSCI World Index



Source: Bloomberg

TECHNOLOGY

Forbes estimates that, by 2035, artificial intelligence (AI) will provide a $14 trillion economic boost to the global economy and increase corporate profitability by 38%. This growth will contribute an additional 1.7% to U.S. annual GDP by 2035. The best opportunities to invest are in the components that make AI possible, including microchips, microprocessors, and graphics processing units (GPU).

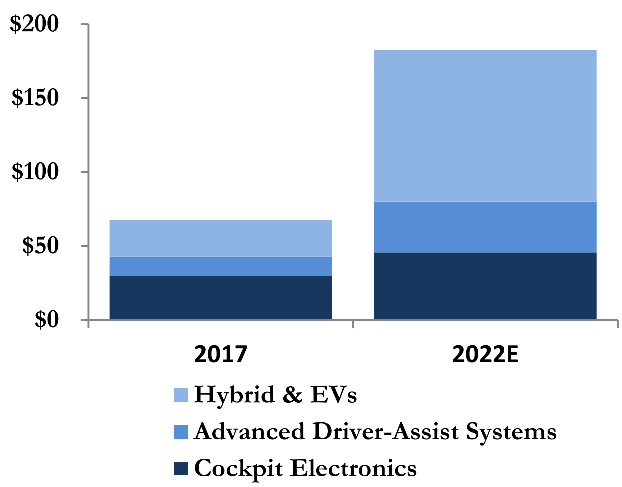
UBS forecasts that the AI chip market will soar from $6 billion to $35 billion by 2021. Most AI-focused chips are developed by U.S. companies.

Amid the growing trend of data-based computing, demand for server-dynamic random-access memory is expected to rise 41% over the next year, according to Citigroup.

The market for specialized auto parts is expected to triple by 2022.

As the sharing economy unfolds, consumers are moving toward owning less and sharing more. The sharing economy continues to drive increases in efficiency across many industries. Cloud computing has allowed individuals and organizations to lease IT services and products, paying only for what they actually use, which researchers have found results in energy savings of more than 80%. Currently, only 17% of companies use the cloud. It is estimated that the total cloud market will grow 30% per year over the next five years.

Revenue from Specialized Auto Parts ($B)



Source: Wall Street Journal, IHS Markit

ELECTRIC VEHICLES

We are in a period of fundamental transformation that is expected to last 10 to 15 years, according to the research firm IHS Markit. This transition will include seeing cars become driverless and the development of transportation as a service. What's more, the growth of electric and autonomous vehicles will drive demand for new specialized automotive parts. The overall market for cockpit electronics, crash-avoidance and advanced driver-assist systems, and components for hybrid and EVs will nearly triple to $183 billion by 2022, as is shown in the accompanying chart. We are looking to invest in those select companies that make critical components for future auto technologies.

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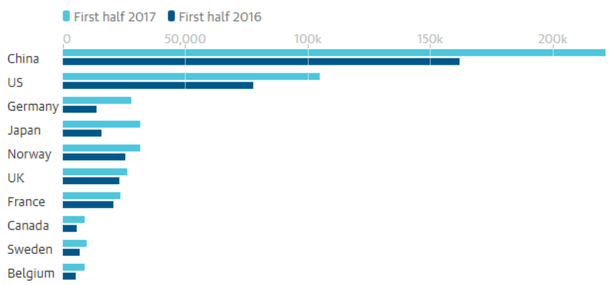
The United Kingdom has signaled its intention to become a leader in the development of fully autonomous vehicles, which means it must move up several levels (as is evidenced by the chart on page 4). By 2021, the UK government would like to see fully autonomous vehicles on the road. The UK has also announced it will be funding £340 million for vehicle purchase subsidies and a national charging network. While the country's Law Commission will be developing legislation to promote the safe use of fully autonomous vehicles, on the manufacturing side, the UK's largest car company, Jaguar Land Rover, has already begun testing its fully autonomous vehicles on British roads.

In November 2017, Uber struck a deal, valued at $1 billion, with Volvo for 24,000 custom SUVs in a bid to create an entire fleet of fully autonomous vehicles. While Volvo hopes to build its fleet of autonomous vehicles, Uber is signaling that its future will largely depend on self-driving cars.

Electric Car Sales by Country



Source: The Guardian

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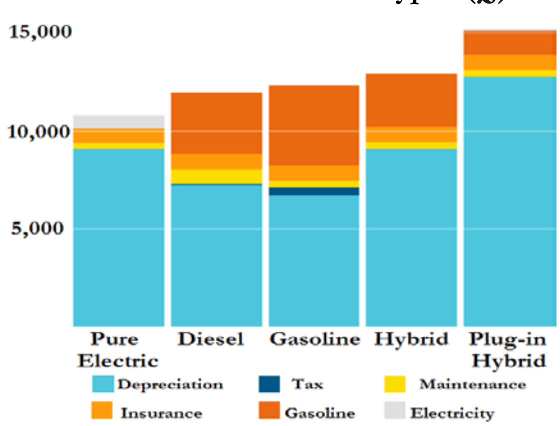
In some cases, electric cars are already cheaper to own and run than gas or diesel models. Total ownership costs per four years for pure electric cars is lower than gas or diesel cars in the UK, the U.S., and Japan, researchers say, but China appears set to lead the market.

In the UK, the annual cost for these new options was about 10% lower than for gas or diesel cars in 2015, the latest year analyzed. The largest contributors to lower annual costs of ownership are the cheaper insurance and the low cost of the efficient electric "fuel."

Annual Cost of Vehicle Types (£)



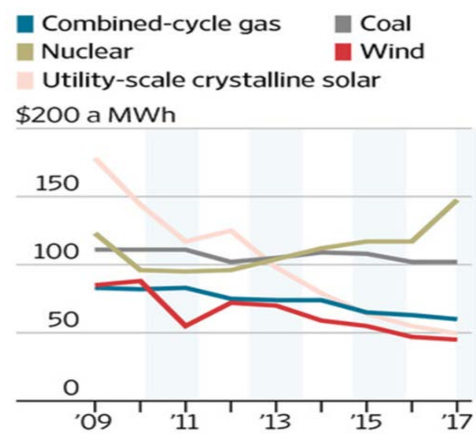
Source: The Guardian

CLEAN ENERGY AND TAX REFORM

Wind and solar are clearly the least expensive and that advantage is driving their growth. The existing tax credits for renewable energy were unaffected by the tax reform bill. Operating projects will be more valuable with the new lower corporate tax rates.

The lower tax rate will reduce the amount of tax equity that can be raised to help finance wind, solar, and other renewable energy projects. Tax equity accounts currently for 50% to 60% of the capital stack for a typical wind farm and 40% to 50% for a typical solar project. The relative value of five important energy sources over the past 8 years can be seen in the chart below.

Comparative Cost of Energy Sources

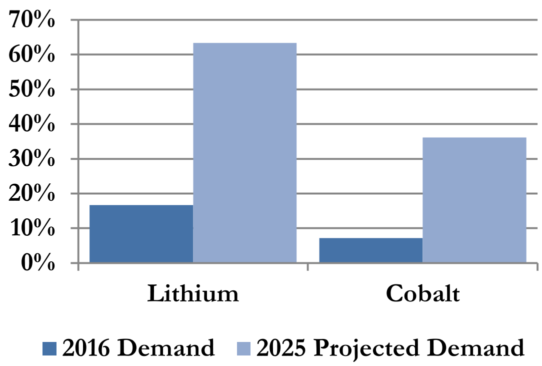


Source: Wall Street Journal

CLEAN ENERGY COMMODITIES

Plug-in hybrids and electric cars create different demands for metals than do conventional cars. Thus, with the change to this new type of transportation, there will be less demand for steel and more demand for aluminum and other lightweight materials. Additionally, fully or partially electric-powered vehicles need more copper for the electric motors on all four wheels, as well as larger wiring harnesses to connect the electric power. Plug-in hybrids need twice the amount of copper compared to conventional cars; electric vehicles need 50% more than plug-in hybrids. Electric and hybrid cars also need more lithium and cobalt for their lithium ion batteries. The EV lithium demand is expected to triple to more than 60% of global lithium production over the next nine years. We favor lithium investments over cobalt because it is forecast to be in short supply and is mined in countries with favorable mining jurisdictions, unlike cobalt.

EV Share of Global Lithium and Cobalt Demand



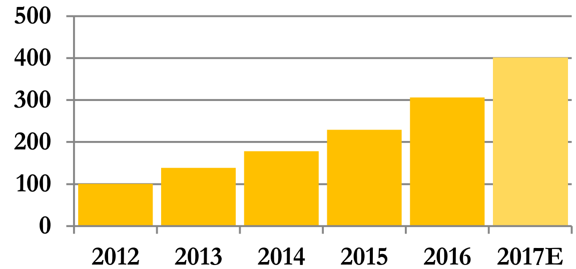
Source: Morgan Stanley, Wall Street Journal

SOLAR

Solar grew 31% for 2017, bringing the estimated cumulative total capacity to 401.5 GW of capacity. It is forecast to grow at 3% in 2018, followed by a 15% increase in 2019.

Solar stocks significantly outperformed the overall equity market in 2017, with the broad solar index increasing by 54%. One reason for this is that China saw an 83% increase in solar capacity, adding 43 GW to capacity. China's acceleration in solar production has allowed the country to already reach its 2020 goal of 105 GW capacity. The country has now increased its goal for 2020 to 213 GW.

GW of Global Solar Capacity



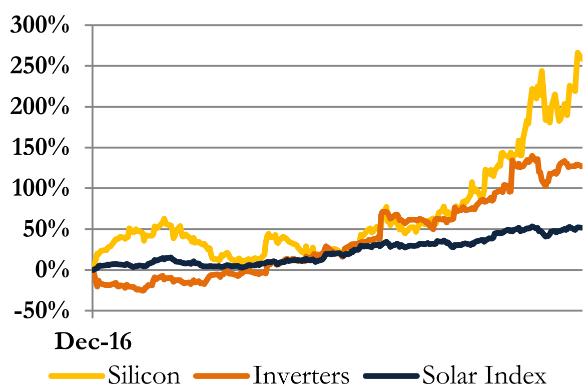
Source: IEA

In the past year, global demand for solar panels grew by 25% year over year. While this shows the strength of the solar sector, a closer look reveals that the top performers were polysilicon and inverter companies, critical components in the solar value chain.

EDF will be investing $25 billion in solar to add 30 GW by 2025.

Competition has been high among solar panel producers, driving down prices and squeezing margins to commodity-like levels. Specialized components such as power inverters continued to offer differentiated technologies that protect them from commoditization. Chinese polysilicon manufacturers also benefited from a policy change, which placed tariffs on imports. The strong growth in demand also led to rising polysilicon prices.

Solar Stock and Index Performance



Source: Bloomberg

In a stunning rebuke for nuclear energy, France's largest utility, Électricité de France, announced it will be investing $25 billion in solar, which will add 30 GW of power by 2025. Nuclear energy currently provides 80% of France's electricity, but it is no longer economically competitive.

PRIVATE EQUITY

While we have made investments in closely-held companies in the past, private equity has become a new focus for us. These are an extension of our work on essential services and essential technologies, including food, water, energy, transportation and waste management. We added Rob Cunjak, formerly of Bain Capital, as a portfolio manager to help us assess and develop our private equity investments.

In December, we invested in EMOH in our growth-oriented products. It is a disruptive water technology company with a near-term path to profitability. EMOH owns a patent-pending proprietary device for low-cost water remediation that has many applications in agriculture and reverse osmosis. The core technology originates from Nikola Tesla's unpublished notes on magnet orientation to create electrolysis. This process produces free oxygen to turn anaerobic ponds into aerobic ponds and produces free hydrogen to bond with nitrogen to create ammonia, resulting in grey water that can then be used on crops.

Through our proprietary network, we also identified a company that specializes in lightweight materials for various end markets, including automotive, aerospace, and consumer products. These metals are two-to-five times stronger and less than half the weight of conventional metals. This investment provides a compelling risk-reward profile, with the benefit of two compelling business lines that provide diversification and a level of downside protection that is atypical of earlier-stage ventures. This company's experienced management team led by a successful serial entrepreneur is making substantial cash investment in the current round. The company's strategic partners provide additional validation of our investment thesis.

CONCLUSION

The stock market performed well in both the fourth quarter and calendar year 2017. Tailwinds are helping drive the markets, as major tax reforms give way to increasing corporate earnings. U.S. manufacturing companies are also benefiting from favorable exchange rates. Tax reform also paves the way for the repatriation of capital held abroad, with some major companies already taking steps to bring capital back, which can be used for mergers and acquisitions, buybacks, capital expenditures and dividend increases.

As the sharing economy unfolds, consumers are moving toward owning less and sharing more.

Interest rates are expected to rise as central banks unwind their quantitative easing programs. Higher interest rates are expected to lead to losses on bond investments and lower real estate prices.

We are in a transformational era where technology is leading to changes and reformation of broad sectors of the economy. We remain focused on the opportunities created by those essential technologies and essential services in both our public and private investments in the belief that they will provide strong returns and stability in these uncertain times.

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