MRP THEMES: REVIEW OF OUR CHANGE-DRIVEN THEMES

Market Viewpoint: October 31, 2018

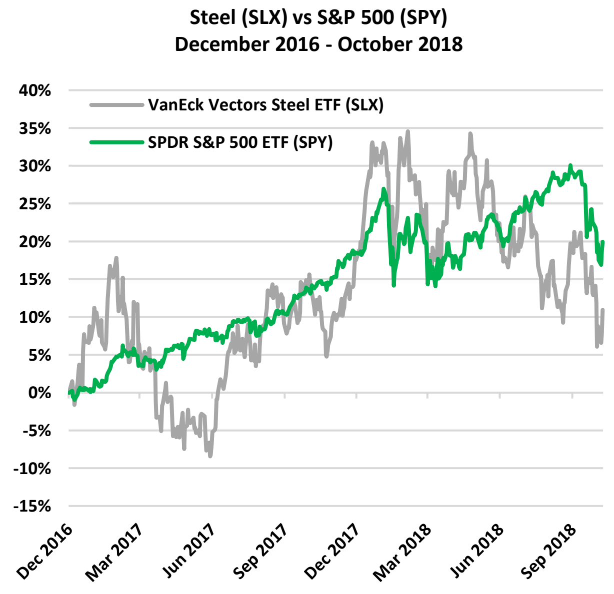
Summary: A series of individual reviews for each active MRP theme, as well as a look back on recently closed themes.

The U.S. capital markets have not been having their best year; and definitely not their best October. A seemingly unstoppable bull market has given way to volatility and equity markets have come very close to falling into correction mode. Interest rates which had been low for so many years are rising: the fed funds rate is up by 75 basis points this year alone, and by a cumulative 200 basis points since the Fed began raising rates two years ago; the 10-year treasury is now well above the 3%-mark, trading about one third higher than at year-end 2017. Equities, after being in a roaring bull market for a decade, have stalled this month, as the S&P 500 has shed over 7% and the CBOE Volatility Index (VIX) has roughly doubled in one month. It is indeed possible that the great bull market is finally giving in to rising rates and extended valuations after repeatedly running up all-time highs in the last 9 and a half years.

MRP believes professional investors would be well-served to focus on themes in all market environments. It is the identification of change-driven themes that is our mission at MRP. So, in the face of the recent market turmoil, an update of our own themes is in order. Since March we have added 6 new themes and also eliminated 6. Currently, we have a total of 22 themes that are active. A review of all those active themes follows.

LONG Steel

The outlook for steel remains positive in the US and in other major steel-producing markets. NAFTA's newly-announced successor, the US-Mexico-Canada Agreement (USMCA), will not eliminate the US's import tariffs on steel and aluminum products from its neighbors. Although some still expect a deal to eliminate the tariffs before the USMCA is signed into law in November, President Trump and Commerce Secretary Ross have not indicated anything to that effect. Trump did, however, state that quotas could eventually replace the tariffs, as long as the US steel industry remains "protected". Argentina, Brazil, and South Korea have already accepted volume limits for their steel exports to the US.



Joseph J. McAlinden, CFA, is the founder of McAlinden Research Partners (MRP) and its parent company, Catalpa Capital Advisors. He has 50 years of investment experience. Mr. McAlinden founded Catalpa Capital in March 2007 after leaving Morgan Stanley Investment Management where he had spent 12 years, serving first as chief investment officer and later as chief global strategist. During his 10 year tenure as chief investment officer, he was responsible for directing MSIM's daily investment activities and oversaw more than $400 billion in assets. As chief global strategist, he developed and articulated the firm's investment policy and outlook. Prior to Morgan Stanley, Mr. McAlinden held positions as chief investment officer at Dillon Read and as President & CEO of Argus Research.

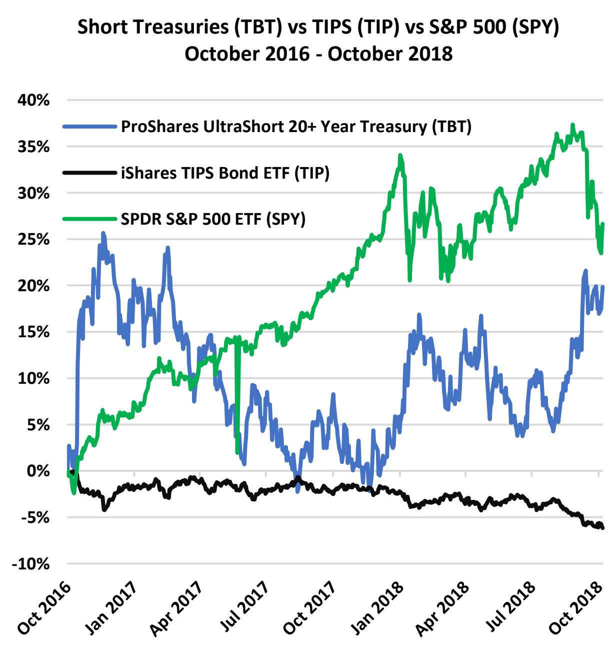
The U.S. steel industry is seeing a "renaissance," according to Industrial Info Resources, as leading players post record profits and American steel prices approach a decade high, rising about 37% in 2018 while US steel imports have fallen 13.5% YoY between April and August.

Whatever the sentiment among their downstream consumers, steel producers are upbeat about the Trump administration's tariffs and expect the growth to continue. Industrial Info is tracking more than $3.7 billion worth of active US steel mill projects that are set to begin construction in the fourth quarter. Additionally, Steelmaker ArcelorMittal expects high, metallurgical coke production in North America to support coking coal markets through 2019. This news comes just as coking coal, an essential ingredient in finished steel, is expected to enter a period of tighter supply as futures prices for 2020 and 2021 have risen substantially since the beginning of the year.

Thanks to China's supply-side reforms and trade actions by several countries, notably including India, Chinese steel exports have come down steadily over the last couple of years. In the first five months of 2018, for instance, China's steel exports stood at 28.5 million tons, declining 16.3% compared with the same period last year. **Launched December 23, 2016.**

LONG TIPS / SHORT Long-Dated US Treasuries

As yields rose across the curve, bond prices fell. The 10-year Treasury note yield rose to 3.22%, its highest level in seven years, and a significant jump from a year ago when they were just above 2%.



We've seen this before. As you may recall, a similar market storm erupted in Jan/Feb 2018 when robust U.S. economic data and optimism about global growth provided a boost to bond yields and pulled the rug out from under the stock market bulls. At the time, MRP wrote: "in the short term, treasury yields will stabilize around 3% for a while, Q1 earnings will be a blow out, and the stock market will rally and make a possible double top sometime in Q2. But, when interest rates resume their upward path, volatility will emerge once again."

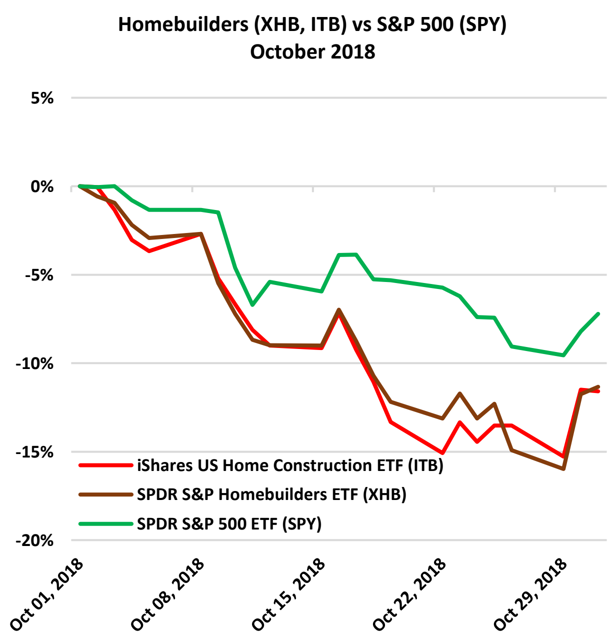
Meanwhile, the U.S. Treasury is expected to issue $1.3 trillion of paper over the next 12 months to fund its trillion-dollar budget deficit. The increased supply should increase borrowing costs further.

A rising interest rate cycle has not occurred in a very long time and the market has gotten complacent about whether the Fed will stick to its interest rate normalization path. Per the latest FOMC report, the Fed expects to raise the federal funds rate one more time in 2018 followed by three rate hikes in 2019. Yet, the market was still pricing in just two rate hikes for next year. Last month's jolt suggests traders are finally starting to believe that the Fed intends to take away the punchbowl. **Launched October 26, 2016.**

SHORT U.S. Homebuilders & Home Construction

After rising for several years, the trendline for the NAHB confidence index has recently reversed course. While the current index level of 68 is considered still "solid," by the industry group, it is now almost 9% below the cycle high of 74 reached in December, and a full point below the full-year average for 2017.

Last month, the Realtor Buyer Traffic Index published by the National Association of Realtors (NAR) slid to 51, a decrease of over 19% YoY, following a 17% drop in August. The Seller Traffic Index also decreased, falling to 41 in September, down from 45 in September 2017. Annual home-price gains fell below 6% for the first time in a year in August.



While there was a slight rebound in sales of new U.S. single family homes in August, sales fell to a near two-year low in September and data for the prior three months was revised lower. Sales of previously owned U.S. homes eased to the weakest pace in almost three years, marking six consecutive months of decline. Meanwhile, pending home sales rose 0.5% MoM, but continued to fall on an annual basis by 1.0%, the ninth consecutive month of declines.

Declining affordability, slower price growth, as well as high regulatory and material costs play are also playing a large role. Prospective buyers are being further dissuaded from buying since, for the first time since 2010, it is now cheaper to rent a home than to be a homeowner in America. **Launched October 1, 2018.**

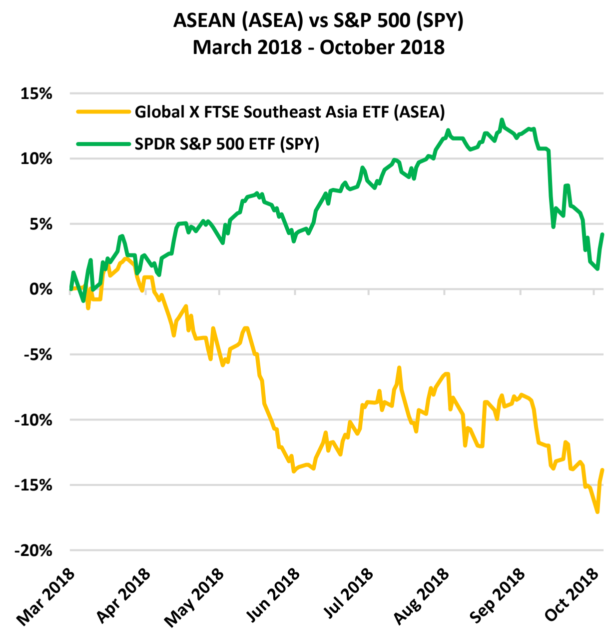
LONG ASEAN

ASEAN had been outperforming the market strongly before Trump's trade war began. However, Southeast Asia could serve as a haven for multinational companies that can no longer afford production operations in China, setting up a unique opportunity to redefine the Asian supply chain.

About one-third of more than 430 American companies in China have or are considering moving production sites abroad amid the tensions, and Southeast Asia ranked as their top destination, according to a survey by AmCham China/Shanghai. An additional survey of about 200 European businesses found that nearly 54% of them feel the US tariffs will cause significant disruptions to the global supply chain and some 7% have either moved or are planning to move their production out of the Chinese mainland. And that percentage could rise as some companies were still assessing the impact from the trade war before they make their decision. Although the latter survey did not ask for a preferred destination, one can assume that Southeast Asia would be high on their list of relocation sites as well.

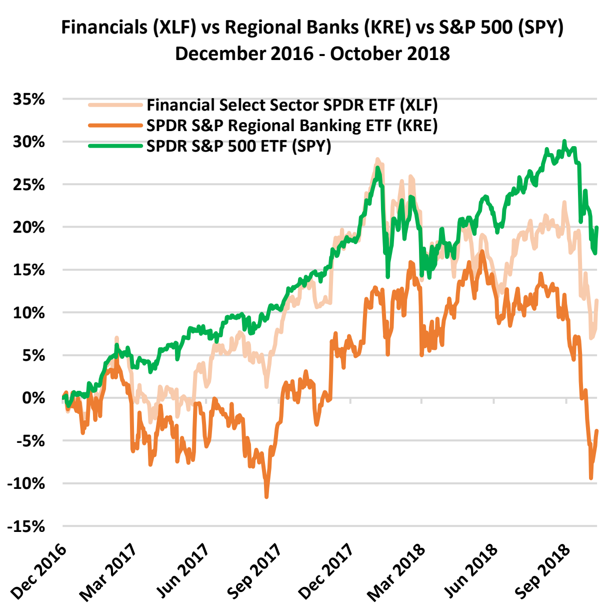
Vietnamese furniture producer Phu Tai, a maker of home furnishings for Wal-Mart Stores outlets in the US is planning for a 30% increase in its exports this year and in 2019, investing about $10 million to expand two factories. Additionally, an executive from Taiwanese notebook PC maker Compal has said that the company is also considering expanding production at facilities in Vietnam.

ASEAN's production continues to gain ground on China's. The manufacturing production index compiled by the Japan Center for Economic Research shows 6.2% year-on-year growth for five key Southeast Asian countries as a weighted average for the January-June period, just shy of China's 6.9%. Moreover, Additionally, ASEAN member states and several other Asia-Pacific economies are currently at the precipice of signing the largest free trade deal in the world. The Regional Comprehensive Economic Partnership (RCEP) encompasses 25% of global gross domestic product (GDP), 45% of the world's total population, 30% of global income and 30% of global trade. Leaders are now set to sign off on a broad agreement of the trade deal at the Singapore ASEAN Summit in November. **Launched March 28, 2018.**



LONG U.S. FINANCIALS & REGIONAL BANKS

In addition to the deregulation that the Trump administration has already been able to pass, this year, more assistance, may be on the way for large and mid-sized banks alike.



The Fed is preparing to revise asset size and other thresholds in its capital and liquidity rules, as part of a series of rule changes under consideration, easing regulatory costs for some large U.S. banks. Other parts of the Trump administration's move to revamp bank regulations include a proposed rewrite of the Volcker rule's trading restrictions in May and an April proposal to alter a big-bank capital rule known as the leverage ratio. Due to the Trump administrations sweeping tax reform bill that was passed at the end of 2017, regional bank executives saw a sudden and notable pick up in both commercial loan demand and spending on credit and debit cards. Commercial and industrial loans were also stronger, with growth that peaked at 6.5%, versus 2017's growth of under 5%.

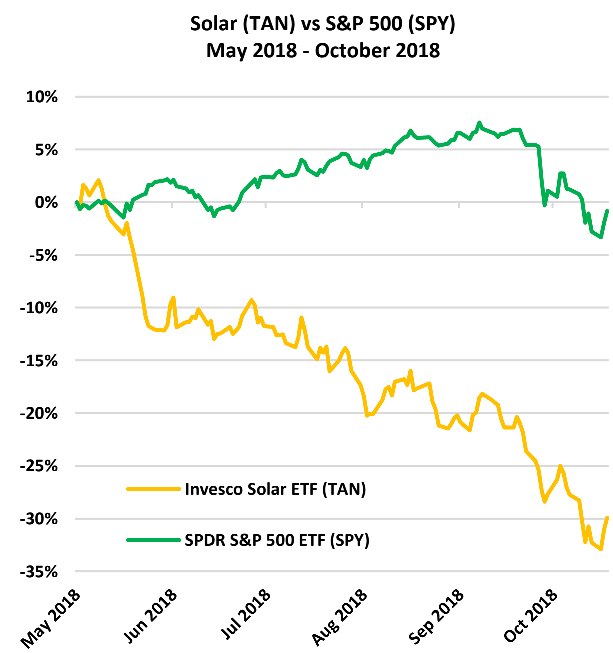
In 2017, there were 252 M&A transactions among US banks, while YTD through June 2018, regional bank and thrift mergers had totaled 259 mergers in less than half the time.

Just as the NFIB's small business optimism index has reached its highest level in 45 years, community bank lending to SMBs increased from 2013 through 2017 by 5%, and that total business lending by all community banks grew to exceed 2010 levels. The US Government Accountability Office has reported that community banks' total business loans outstanding increased during that time frame, from $689 billion in 2010 to about $765 billion in 2017, or approximately 11%. This could be significant to regional banks looking to acquire smaller community counterparts since the acquirer will also have a good chance to usurp and maintain the community bank's prior lending relationships as well. **Launched December 23, 2016.**

LONG Solar

New legislation has been introduced in California, mandating utilities to buy approximately 2,500 megawatts of wind and solar power over the next four years before certain federal tax credits expire. New York has unveiled higher incentives for solar projects on landfills and brownfields to help meet the state's goal of 50% renewable energy by 2030. The Texas power grid is also going green at an increasing rate, as new solar plants in the state are being planned regularly. In Michigan and Colorado, the largest utilities are phasing out coal to be replaced by renewables.

Meanwhile, corporate procurement activity is accelerating as more large-scale power buyers such as Google, Facebook and Apple prioritize clean energy. By the first half of 2018, corporations had already purchased more renewable power than they did in all of 2017, with the U.S. and Nordic countries accounting for almost 80% of this year's activity. The number of industries involved in clean energy purchases continues to grow. AT&T, for instance, has just spearheaded a push for American telecom companies to buy clean energy.



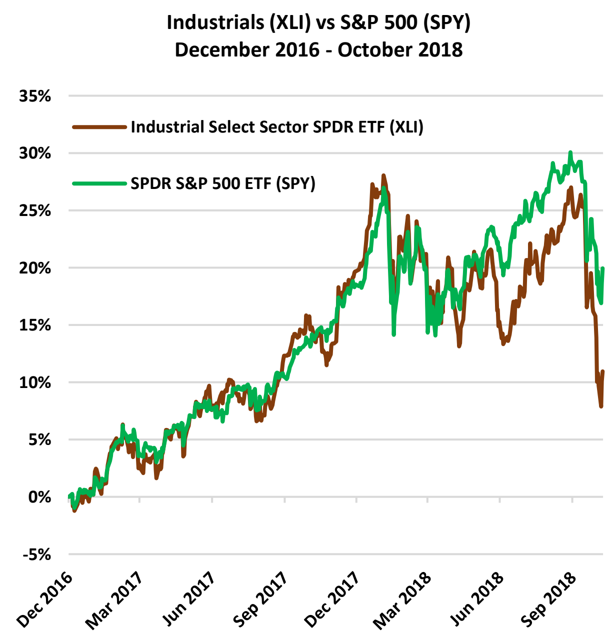
Even the U.S. military is increasing its investments in solar power. Cyberattacks and natural disasters have revealed vulnerabilities in the traditional power grid and the need to develop a "self-resupplying power source," according to Michael McGhee, who leads the US Army's Office of Energy Initiatives.

New regional markets are also opening up outside of North America, Europe and Asia. Africa is poised to become an emerging force in solar thanks to initiatives like the World Bank's 'Scaling Solar' program which is facilitating large scale solar projects at low prices across sub-Saharan Africa. In the Middle East, Saudi Arabia and United Arab Emirates (UAE) are two new ambitious additions to the industry. The Saudi solar market is expected to expand at a CAGR of 30% between 2018 and 2024, whereas the UAE pans to source a quarter of its energy from solar installations by 2030.

All the while, the fundamental economics of the industry are changing rapidly as the cost-competitiveness improves, especially in light of this year's run-up in crude prices. Solar power will become cheaper than conventional sources of electricity generation by 2020. **Launched May 14, 2018.**

LONG Industrials

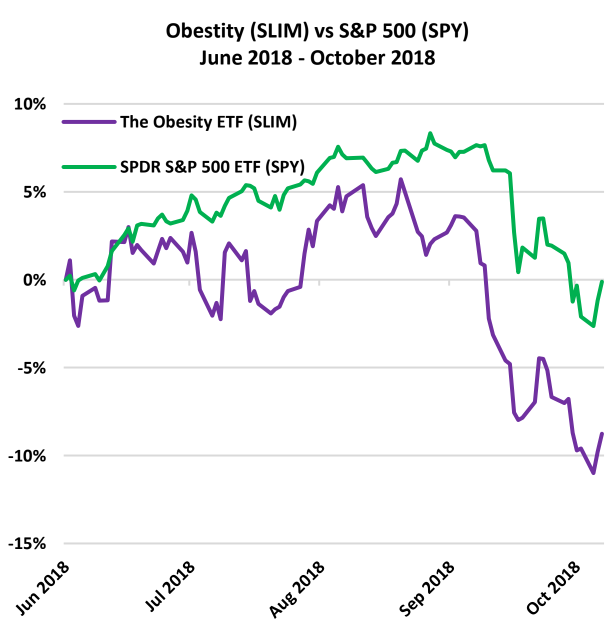
Industrial production — a gauge of output at factories, mines, utilities and the like — rose 0.3% month-on-month in September, exceeding expectations, and marked the fourth consecutive monthly rise. New orders for durable goods jumped 4.5% in August, boosted by a 69.1% surge in nondefense aircraft and a 17.0% gain in defense aircraft. Additionally, the Philadelphia Fed Manufacturing Index rose strongly to 22.9 in September from 11.9 in August.



Meanwhile the September 2018 IHS Markit PEG Engineering and Construction Cost Index report revealed that construction costs rose at an accelerated pace month-over-month to an index reading of 62.1 — up 3.2 points from August. This marks the 23rd straight month of cost increases. Capital investments, which includes money spent to upgrade physical equipment such as buildings, equipment and machinery, jumped up to $341 billion in the first half of the year, an increase of $55 billion, or 19%. **Launched December 23, 2016.**

LONG Obesity

In America, the obesity rate is on the rise again after briefly leveling off in recent years. At this point, more than a third of rural residents qualify as obese while the rate in metropolitan areas is about 28.7%. Internationally, three in five Britons are overweight or obese, according to a 2017 report by the Organization for Economic Co-operation and Development (OECD). Childhood obesity in southern European countries was twice as prevalent than in northern European countries such as Denmark, Ireland and Norway, where rates of obesity in boys and girls ranged between 5% and 9%.



The biggest name in weight loss, Weight Watchers, recently rebranded to "WW" and is now dedicated to delivering a broader approach to wellness than just weight loss plans, focusing on shifting to a "technology experience company"; even relisting on the NASDAQ. This is consistent with the broader sector transition toward more tech-based applications.

Novo-Nordisk is a more healthcare-oriented company that is following a similar path as WW, leveraging their huge information database to generate individual-specific treatments that suppress energy intake and increase energy expenditure. These sorts of treatments would be delivered via injection, oral treatments, and combinations of different therapies.

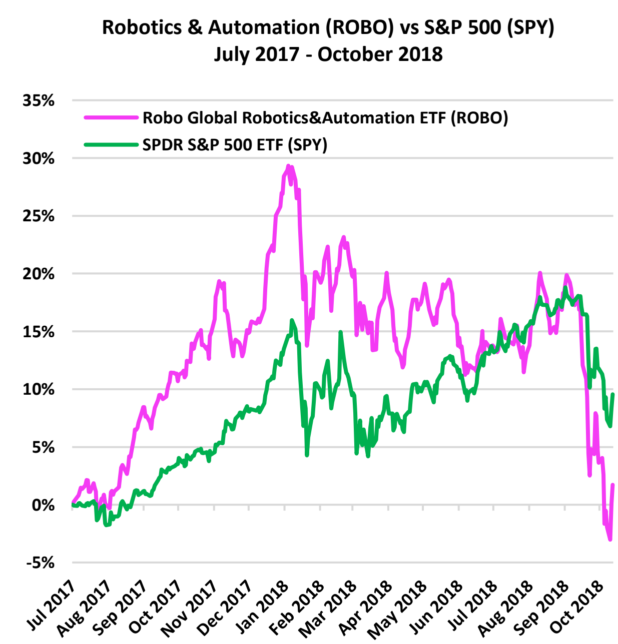
Obesity rates should continue to rise in the short term and the market for treatments should grow alongside it, and even more so when the trend in obesity begins to reverse and doctors get a strong hold on what works. **Launched June 25, 2018.**

LONG Robotics and Automation

In August, Softbank entered talks with startup Zume, offering a blockbuster investment of anywhere from $500 million to $700 million. Zume's product? A fully automated pizza delivery service. And Zume isn't alone in their quest for fast food optimization. Yum! Brands Inc.'s Pizza Hut and Dominoes have experimented with robots as well. Beyond Pizza, chain brands like Subway and McDonald's, have been rolling out plans to transform thousands of restaurant locations nationwide, boasting new designs and layouts of stores.

Consulting firm Deloitte estimates that "assets under automated management" (yes, "AUAM" is now a thing) in the U.S. will grow to $5-$7 trillion by the year 2025 from about $300 billion today and $100 billion in 2016. That would represent between 10% and 15% of total retail financial assets under management, which is why traditional retail investment giants Schwab, Vanguard, Morgan Stanley, BlackRock, and others have rushed to develop their own robo-advisors.

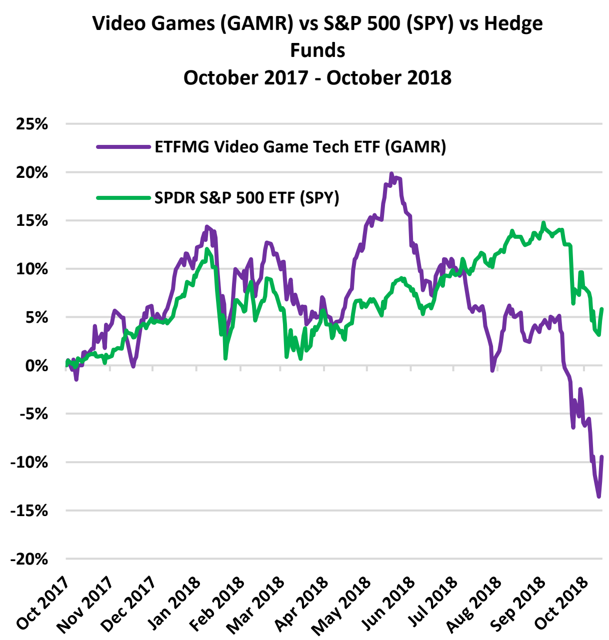
Shimizu Corp., a Japanese general contractor, is becoming one of the first to implement robotics-based solutions by introducing robots that can weld beams, haul supplies and install ceiling panels. Shimizu's Robo-Carrier automated forklifts will be equipped with laser rangefinders to navigate environments and their Robo-Buddy will be able to lift and carry 30 kilograms of materials at a time.



Workers at a Colorado masonry company were recently introduced to a bricklaying robot worker named SAM, or Semi-Automated Mason that can lay 3,000 bricks in a typical eight-hour workday. Similar machines could be used to automate similar routine tasks with some human oversight. Hadrian X by Fastbrick Robotics, a similar bot equipped with specialized technology, can lay a residential house from the ground up, on site, in 2 days.
Launched July 20, 2017.

LONG Video Gaming

In June, video games officially became the world's most popular form of entertainment. According to Reuters, gaming grew by 10.7% during the last year alone, while television continued its steady decline with an 8% drop globally.



Overall video games sales rose 26% in August to $796M, according to NPD Group. Software sales rose 16% to $330M; hardware sales increased 28% to $214M. Argos reports that gaming laptop and headset sales are up 62% and 65%, respectively, this year. When all is said and done, total revenue video games and related fare are predicted to generate close to $140 billion this year, an increase of more than 13% from 2017, according to VanEck.

MRP has been focusing on gaming's transition to the cloud to propel the sector further. Jeffries predicts that, by 2020, 75% of new console games will be downloaded, versus under 40% today. That will push margins even higher—an estimated three percentage points of gross-margin increase for each 10%age points of added download penetration.

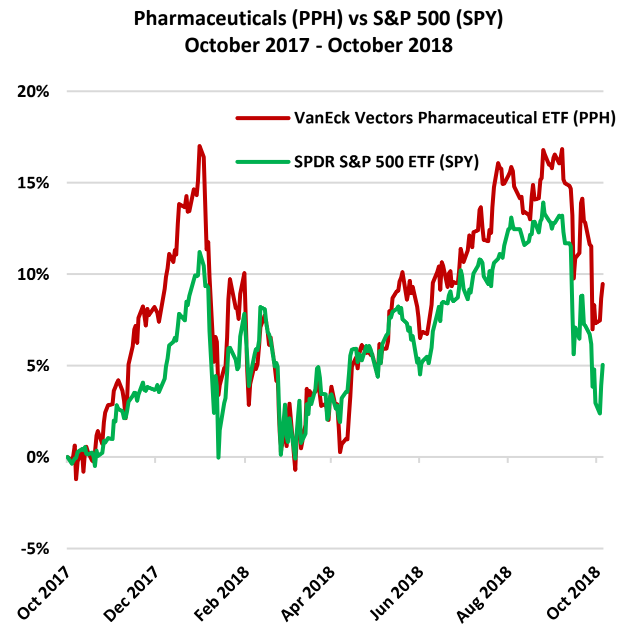
Analysts expect EA to introduce a subscription-based cloud service for playing AAA games within two to three years. That will correspond with the rise of fifth-generation cellular service, or 5G, which will begin rolling out later this year as fixed broadband connections and next year as mobile broadband. It will not only increase data speeds, but also reduce latency, including on mobile devices. 5G is also likely to make next gen virtual reality games less cost-prohibitive. When complex computing can be rerouted to the cloud (thanks to faster connections), it takes that stress of home devices, thereby making them more widely available at lower price points.

Video Gaming has taken a hit as of late, due to financial turbulence in a couple of the larger companies in the sector, however, it has not disrupted the longer-term fundamental transformations MRP is anticipating in the sector. **Launched October 19, 2017.**

SHORT Pharmaceuticals

Recently, the Trump administration released new guidance for Medicare Advantage plans, the private insurance alternatives to traditional Medicare that cover about 20 million seniors. The goal is to create leverage to negotiate lower prices from drug makers via prior authorization, which would require doctors to receive permission from the insurance company before prescribing a medication to their patient; as well as step therapy, which has patients start with cheaper (and typically weaker) medications and move to stronger, more expensive drugs only if the cheaper alternative doesn't work.

The Administration also announced a plan to narrow the gap between U.S. drug prices and those of other countries. The strategy concentrates on drugs administered by doctors — mainly the newer, very expensive biologic drugs that treat cancer and chronic conditions such as arthritis and macular degeneration. Medicare's prices for these drugs are nearly double the average paid in Europe, Japan and Canada. To close the gap, the Trump administration would benchmark Medicare payments to the average foreign price. The Administration estimates that implementation of the new pricing index would save Medicare $17.2 billion over a five year period.

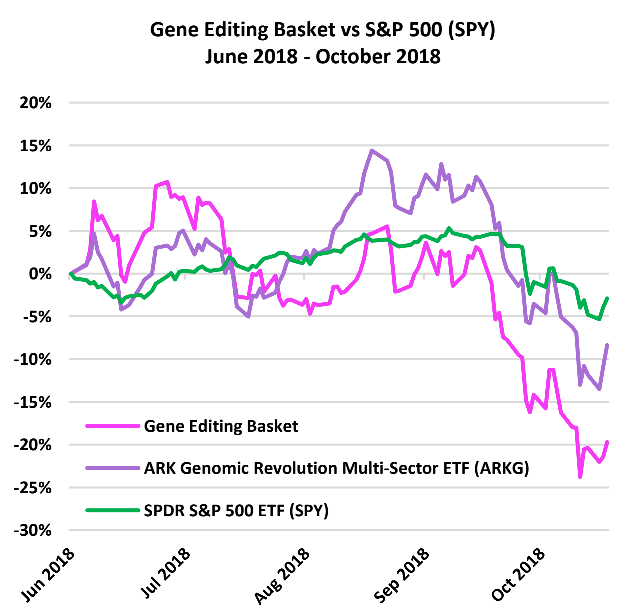


Soon, the Trump administration will also require drug companies to disclose the list price of medications in their direct-to-consumer advertising, that fact will become abundantly clear to policymakers and the American people alike. Just as patients need to know about the possible side effects of a drug, they also need to know how much it costs and whether there are more affordable treatments available. In pursuing such transparency, another bill backed by the President, the "Know the Lowest Price Act", will allow pharmacists to tell patients about the cheapest way to pay for prescription drugs at the counter. **Launched October 27, 2017.**

LONG CRISPR

Animal and agricultural scientists have begun to utilize CRISPR/Cas 9 gene editing technology to effectively mimic natural selection, while speeding it up and being more precise in the process. Gene editing can help fight disease in livestock while cutting costs and improving production.

Recent experiments on farm pigs have shown that gene editing is a way to get rid of harmful diseases such as Porcine Reproductive and Respiratory Syndrome. PRRS has been a devastating disease in the U.S. pork industry, in which vaccination hasn't been very effective and air filtration has been a slightly effective tool. Other cattle-based research in China has used CRISPR to create tuberculosis-resistant cattle.



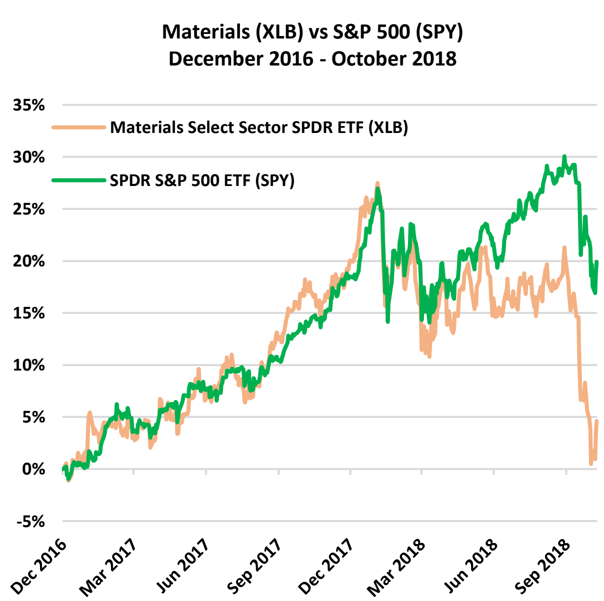
Due to the genetic relationship between the groundcherry, a crop fruit indigenous to Central and South America, and the tomato, researchers could leverage what we already know about the tomato genome to see if similar traits and characteristics could be targeted. The work enabled the researchers to modify the plant to help create more clustered flowering, increasing fruit yields, and larger fruit size. This kind of modification could absolutely be expanded to many other crops as well.

Recently, scientists in China successfully generated offspring using the DNA of two same-sex mammals. The team essentially created pseudo-sperm by mutating the DNA-carrying cell of one female mouse. Combining that with the DNA-carrying cell of another female mouse, they were able to make a fertilized egg which was then implanted into the womb of a surrogate mouse-mom, resulting in a baby mouse. Following that process, the scientists were able to produce 29 live mice from 210 embryos and zero contributions from male mice. The offspring resulting from bimaternal DNA, edited using CRISPR, were found to be healthy and indistinguishable from mice conceived the traditional way.

The most recent significant development in human disease prevention has been the success of scientists at the Children's Hospital of Philadelphia (CHOP) successfully using CRISPR to alter the DNA of laboratory mice in the womb, eliminating an often-fatal liver disease before the animals had even been born. **Launched June 14, 2018.**

LONG Materials

The metals market has suffered However, a in a recent survey conducted by Macquarie, delegates at London Metals Week ranked their metal preferences for the next 12-months in terms of those in which they might take a long position and those they are likely to short. Copper was seen by 45% of respondents as the metal they would most likely buy, followed by nickel with a 31% positive response, indicating improved optimism from a year prior.



Chinese factory output of the metal has also slowed, and exports have declined due to the trade slowdown with the US. The good news, however, is that the country's demand, which accounts for 45% of global copper demand alone, has been so strong in the past few months that top producer Codelco has almost sold out of supplies for next year.

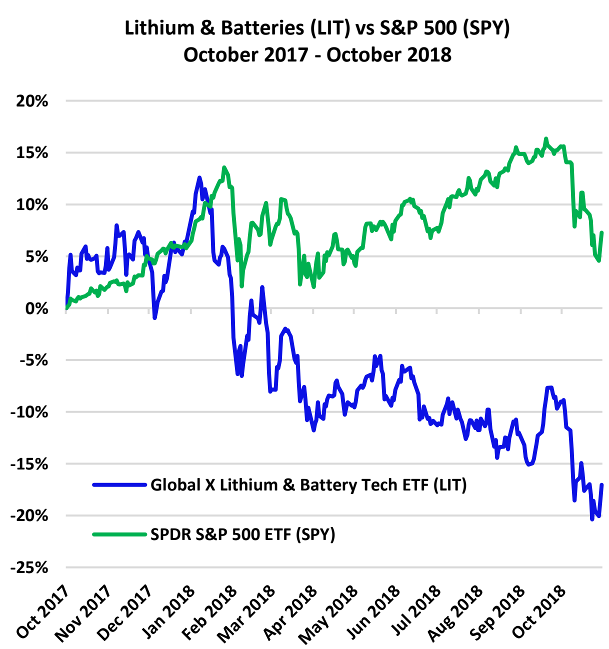
Additionally, the Wall Street Journal reports that Codelco has locked in copper-cathode supply contracts with European buyers at a premium of $98 a metric ton over benchmark prices, the highest since 2015. Premiums for contracts signed this year with clients in China and the U.S. are also up by 15% to 17%.

There have also been optimistic predictions for aluminum, as demand growth has been forecast to more than double by 2025 according to the Vice President of global automotive
at Novelis.

Vanadium, an additive hardening ingredient in finished steel, is another material to watch as China has implemented a new rebar standard to take effect in November 2018. This standard calls for stronger rebar, which means more vanadium will be required in steel production. **Launched December 23, 2016.**

LONG Lithium

Commodity research and consultancy firm, Roskill, has projected demand from companies which produce lithium-ion batteries to power electric cars, laptops and other high-tech devices will grow from 46% of total lithium supplies last year to 83% by 2027. This is an especially significant finding because it follows a similar prediction from CRU Group, which estimated that lithium carbonate equivalent (LCE), the most widely traded of lithium products that goes into the cathodes of lithium-ion batteries used in electric cars, will more than triple between now and 2025. While use of lithium hydroxide (LiOH, a stronger lithium compound that can also be used for batteries) will become more prevalent over time, installing new battery grade capacity has proven complex and could materialize more slowly an expected. As a result, Roskill suggests that an increasing share of demand from battery producers dependent on less energy-dense LCE are one factor that should keep prices strong, even in the short term.



Expectations for lithium supply capacity have disappointed before. 2012 saw thirteen major mining companies from around the world plan to add over 200 ktpa (thousand tonnes per annum) of production by 2016. When 2016 arrived, however, the total amount of added lithium supply from these companies totaled only about 10% of that goal. Only one brine mining project and zero hard rock projects have been put into full production over the last two decades.

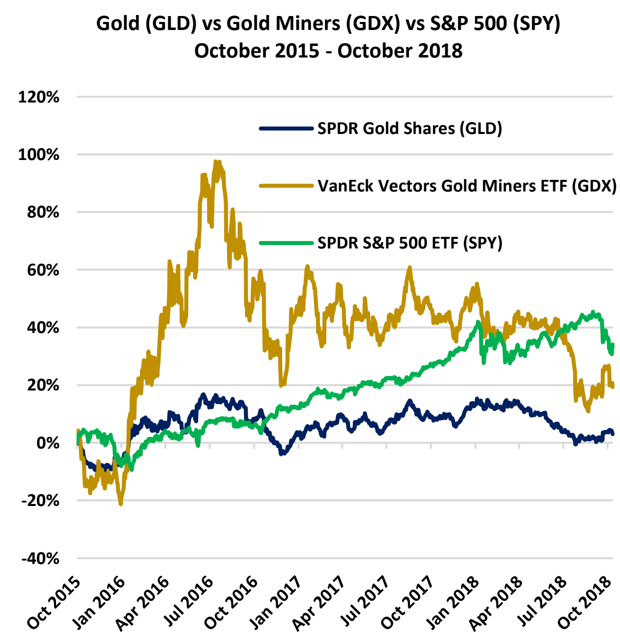
And when done so, it's been by the major lithium producers in just four countries – Chile, Argentina, China and Australia. This exposes something in the industry no one talks about; a lack of skilled personnel to get involved with mineralogy/metallurgy and the engineering of mining projects that many countries are not familiar with.

Pair that track record with a need for up to $12 billion in downstream investment in the industry and a coming decline in lithium intensity – the amount of lithium used per unit of energy the battery produces – that will require a shift to larger battery packs to give EVs the range that consumers demand, measurements of real future supply no longer seem very reliable. **Launched October 21, 2015.**

LONG Gold and Gold Miners

In aggregate, central bank buying is happening at the fastest pace in six years. In the first half of 2018, they added a net total of 193 tons of gold to their reserves – an 8% increase from the 178 tons purchased over the same period last year. By year end, net purchases of gold by central banks are forecast to rise to 450 metric tons this year, up from 375 tons in 2017, according to consultancy Metals Focus Ltd. The first increase since 2013.

The Russian government has been steadily liquidating its US Treasury holdings and buying gold instead. Once among the world's top 10 buyers of US sovereign bonds, Russia's Treasury holdings plunged from $176.3 billion in 2010 to $14.9 billion in May 2018, as Moscow's gold purchases were reaching record highs. In contrast, Russia's gold reserves grew from a record low of 343 tons in the second quarter of 2000 to an all-time high of 1,998.5 tons (64.25 million troy ounces worth $79 billion or nearly 17% of overall Russian reserves) in the third quarter of 2018. China's reserves increased just as dramatically, rising from 395 tons to 1,842.6 tons over the same period. Additionally, Poland added about 9 metric tons to its bullion reserves in July and August. That's Poland's biggest purchase since 1998 and among the largest additions by a European Union nation since then. Hungary has also increased its gold reserves tenfold to 31.5 tons.



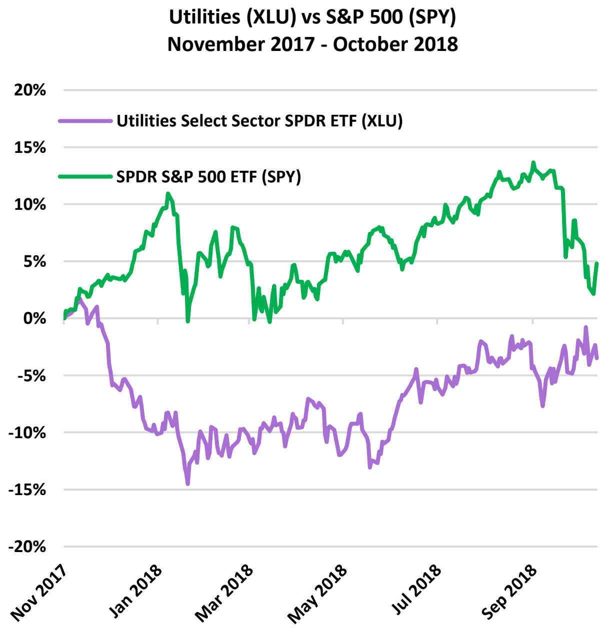
Furthermore, not only has there been a consolidation in the mining sector, but the correlation between the greenback and gold has weakened in recent months, indicating that other drivers - such as haven demand from investors fleeing equities and cryptocurrencies - could continue to firm up bullion prices. MRP does expect to see buoyancy in the dollar for the next few months, followed by weakness next year.

Mining gold has become more difficult. Global discoveries and output is expected to decrease steadily, with many experts now predicting an era of "peak gold." Some industry insiders believe 2017 was the peak point for gold, and they anticipate supply to fall up to 20% by 2022. **Launched October 21, 2015.**

LONG Electric Utilities

Although a rising interest rate environment is rarely good news for utilities, all utilities should not be lumped together; the electric segment has a much brighter outlook for the first time in many years, particularly in places like the United States.

The S&P 500 utility sector is up by 2.3% in October, while every other sector is in the red and the broader index is down by more than 7%. Despite the 10-year yield sitting near a seven-year high, the stock market slump is enough to overcome the headwinds and make investors prioritize another benefit of utility safe haven.



In the longer term, although America's electricity industry has recently struggled with flat demand for power in recent years, the nation is moving towards more electricity consumption, not less. Indeed, the growth of renewable energy, advances in energy storage, cryptocurrency mining, the explosion of connected devices which feed into data centers, and the increase in electric-powered transportation – from scooters, to cars, buses, ships, and even planes - all point to greater electricity consumption going forward. This makes electric utilities a convenient picks-and-shovels play on all these trends.

Increased KWH consumption will not show up much in earnings in the near-term. But the enhanced long-term growth prospects should lead to a re-rating of share valuations; in other words, higher P/E's.

In the U.S. a typical electric car, for example, would use 261 kWh monthly, which could increase that household's demand for electricity by 25 to 40%. In Europe, the revenue opportunity is even greater, as an electric car driven 15,000km per year would approximately double the household's energy use. In preparation, many power companies are already rolling out EV charging infrastructure programs. In California, for example, San Diego Gas, Southern California Edison, and Pacific Gas and Electric plan to build 12,500 charging stations across public locations. In 2016, there were 567,000 electric vehicles (EVs) on the road. But thanks to an EV boom, that number may reach a whopping 7 million cars by 2025. Electric vehicles could account for up to 76% of vehicle-miles traveled by 2050, which would drive a 38% increase in U.S. electricity needs.

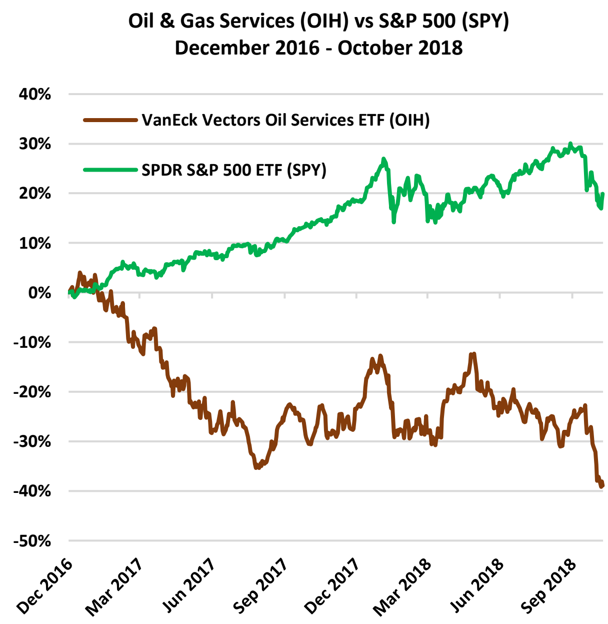
Another new trend in electricity demand is cryptocurrencies. Although the price of bitcoin has fallen strongly over the last year, the electricity consumption of cryptocurrency miners has now risen over 240% YoY, according to Digiconomist's Bitcoin Energy Consumption Index. **Launched November 20, 2017.**

LONG Oil & Gas Services

A glut of oil in the Permian basin, the largest shale field in the world, has pushed local prices close to four-year lows, causing operators to slow down their drilling and production activity, therefore, hurting demand for oilfield services. This issue is a result of underinvestment in energy capex, creating a sizeable pipeline shortage that has strangled the basin's outgoing product while production has doubled. Due to the Permian bottleneck, the basin's crude was selling at as much as an $18 per barrel discount to the U.S. oil benchmark WTI.

To remedy this glut, new capacity is already being added, including Plains All American's opening of a 90,000 barrel per day (bpd) crude oil pipeline expansion by the end of October. And Plains' project is only a drop in the bucket compared to a further $300 billion in capex the Permian will need over the next 5 years to need to keep pace with growth projections.

The Permian's pipeline woes are not an isolated case. Canadian oil futures were averaging a discount spread of nearly $20 against the US WTI benchmark through August due to similar pipeline shortages which will need to be remedied with millions of dollars of investment into installation of new lines.

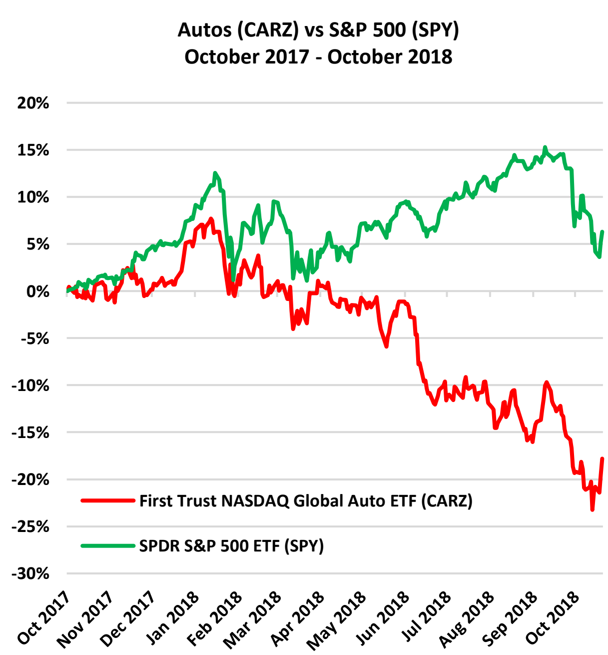


Beyond pipelines, Offshore equipment and service companies are also beginning to open the taps on spending. Transocean Ltd, a top supplier of drilling vessels, said last month that rates for its new high-spec vessels in the North Sea are now fetching $300,000 per day. IHS Markit now expects 2020 global offshore rig demand to average 521 units, up from a 2018 estimate of 453 units. According to Rystad, last year there was a 50% increase YoY in the number of offshore projects sanctioned with 62 financial investment decisions.

Morgan Stanley's view is that broad oil and gas services growth will be sustained around the globe. Last month, they issued a report predicting that oil and gas drillers are on the verge of a worldwide spending spree not seen since 2013. Due to unexpected spending from European oil majors, independent drillers, and Chinese LNG demand, the bank expects capital expenditures to rise 15% through 2020, compared to a measly 5% gain we have seen since 2016. **Launched December 23, 2016.**

SHORT Autos

U.S. interest rates continue to rise, driving up monthly payments on car loans, disincentivizing some buyers and contribute to slower sales. Additionally, huge amounts of auto debt are still being racked up. Auto Loans Outstanding in the second quarter of 2018 totaled $1.238 Trillion, up 4.0% YoY. What's worse, 4.17% of all outstanding loans are seriously delinquent, the second highest level since 2012, and up from 3.92% a year ago. In Q2 2017.



The newest data has also shown that Americans are holding on to their cars and light vehicles longer and longer. The average age of a vehicle bought new rose from 9.3 years in 2009 to 10.5 years in 2017. Obviously, the longer consumers keep their cars, the more it undercuts sales of cars this year and beyond.

Used car prices have also fallen to their lowest level since 2009, declining 1.5% YoY in September. Weak used vehicle prices can hurt consumer demand for new vehicles due to lower trading values

Total vehicle sales in the US market fell 3.4% YoY in September, the largest decline since August 2017. Bottlenecks created by the mandatory changeover to new fuel economy testing standards have begun depressing sales and hurting auto manufacturers in Europe as well as both Volkswagen and Audi's European sales were down over 50% in September compared to year ago numbers. Canadian auto sales saw their seventh straight month of declines in September as the 7.4% drop in the new light vehicles segment was the steepest since 2009. Overall passenger car sales were down 13.7%.

The auto market looks even worse in the emerging economies of Asia. Auto sales in China fell for a third straight month in September, as the country's auto sector saw an 11.6% decline in overall sales YoY. Nomura Securities Co. now expects fourth-quarter sales to fall 7.5%, resulting in a full-year decline of 1.6%, which would be the first annual decline for China's passenger-car market since 1990. The Financial Times' ASEAN auto purchase index (API), which surveys 5,000 ASEAN 5 consumers, has now declined to its lowest level in 3 years. India's top 5 car manufacturers also suffered a 2% drop in sales YoY. **Launched October 12, 2017.**

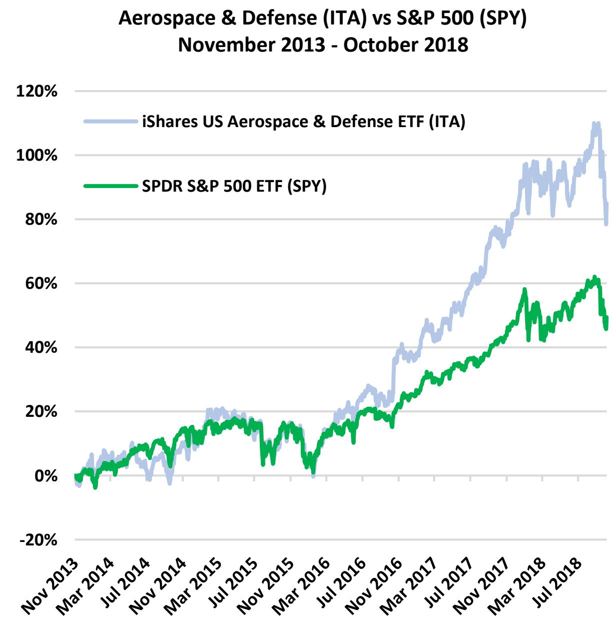
LONG Defense

On August 1st, the US Congress approved the defense budget for 2019. The bill earmarked a record $717 billion to the military. Only days after Senators were putting their signatures on the new budget, China had just finished up a successful test of hypersonic weaponry — projectiles able to travel at least five times the speed of sound, about 3,800mph — becoming the third country, after the US and Russia, known to be developing superfast weaponry. This puts the Chinese military right on the heels of the US, whose efforts thus far have been labeled as "sluggish".

To keep pace in this quiet arms race, the US Missile Defense Agency asked for $120 million in its 2019 budget to develop hypersonic missile defenses, up from $75 million in this year's. Companies are also making headway with lucrative government contracts. Lockheed Martin received a contract from the Air Force in April to build a hypersonic strike weapon that could be launched from fighters and bombers. The company is reported to have invested $100 million in corporate R&D in technologies that would advance hypersonic defense. Boeing has also been working on hypersonic weapons technology for years, and in 2013 a test flight of its X-51 Waverider provided proof that it was feasible.

Additionally, military modernization is shifting more and more to the weaponization of space via satellite technologies. The Trump administration's innovative "Space Force" initiative will require many new military investments. Satellites will be right at the forefront of the Space Force agenda as our older, increasingly obsolete telecommunications infrastructure becomes vulnerable to attacks. It was all the way back in 2007, when China first used a ballistic missile to destroy its own old weather satellite orbiting 535 miles above Earth.

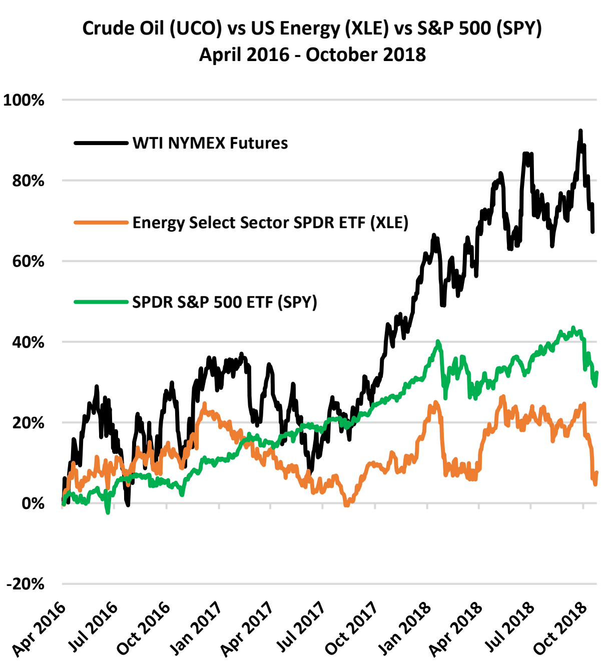
A communications satellite that's jammed from the ground could mean ground troops suddenly find themselves operating blindly. And because existing international treaties governing space are unclear, even civilian satellites could be targeted by nations looking to contain or punish their enemies. As far in the past as 2001, former Secretary of Defense Donald Rumsfeld concluded that the U.S. wasn't prepared to defend its enormous dependence on satellites. A move toward satellite defense would likely benefit both rocket and satellite producers, due to the need for new satellite hardware and software that could resist cyber-attacks, as well as spacecraft that could intercept physical attacks from projectiles. **Launched November 27, 2013.**



LONG Crude and US Energy

Oil has been strong through late September and early October, with WTI holding well above $70 per barrel. Although consecutive supply builds have pulled prices back a bit, that is to be expected during this time of year as drivers are in limbo between summer and the holidays.

The reality is that demand recently reached a landmark level of 100 million barrels per day (BPD), the combined US oil and gas rig count are beginning to decline again, hitting a five-week low of 1,161 in mid-October amid further declines in the Permian Basin, and at the end of September, OPEC and its allies chose to forgo any further increases in oil output.



Additionally, export decline from Iran and Venezuela continue to loom large. Oil exports from Iran fell to their lowest level in 2 1/2 years before the impending return of U.S. sanctions that President Trump hopes will eliminate their export volume to many major markets in Europe and Asia. Venezuela pumped only 1.45 million bpd in August, and the year-to-date average stands at 1.544 million bpd. This is a far cry from the figure from five years ago, when its daily average was 2.9 million bpd.

Earlier in October, a committee of producers including Russia and Saudi Arabia highlighted the need to prepare "options" for how much oil they should pump next year to prevent the market slipping back into imbalance, setting the stage for new production cuts to counter any kind of supply builds toward the end of 2018.

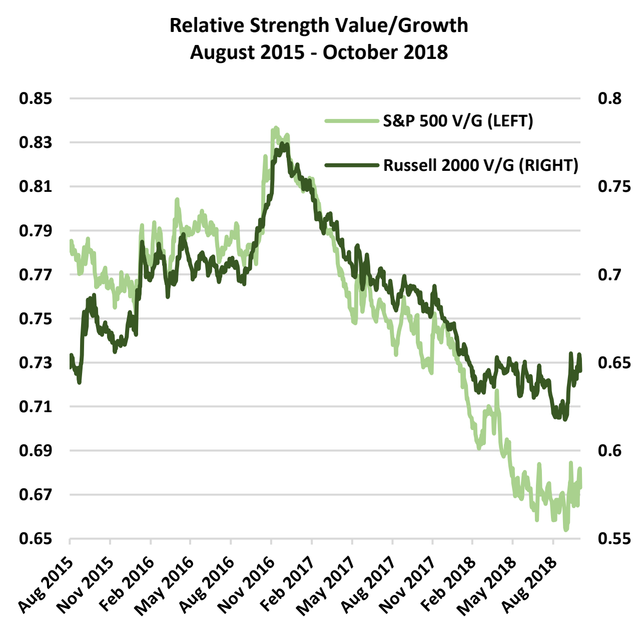
With winter just five weeks away, we will go into winter with the lowest natural gas storage since 2003. The Henry Hub spot price has risen above $3.20 per MMBtu, close to the highest level since January, in anticipation. Despite record U.S. gas production, inventories have not sufficiently rebalanced due to an extraordinarily hot summer, creating a deficit of at least 14% across all regions, according to the EIA.

Asia's liquefied natural gas prices are rising especially fast on tightening supplies and expected strong Chinese demand in the winter. Average Chinese gas import prices jumped 23% compared to a year ago in the second quarter. Japanese contract prices were up 17% in the same period.

Now that rise in crude and natural gas prices has been sustained for some time, we should soon see improved earnings among energy producers third and fourth quarter results. **Launched April 8, 2016.**

LONG Value over Growth

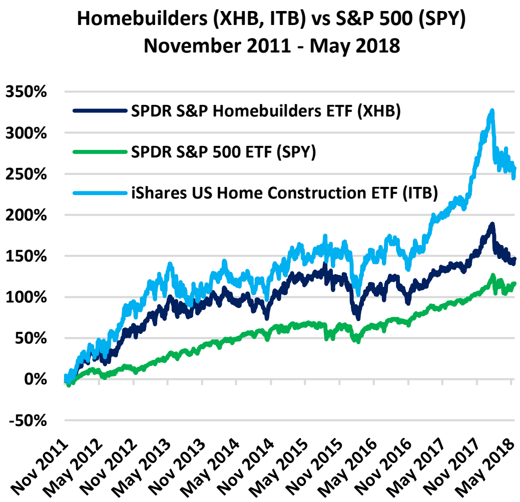
Defensive sectors such as health care and consumer staples have already been the market leaders since early June, while growth sectors such as technology have been lagging. Over the course of the last 3 months, the S&P value ETF (IVE) has begun to outperform the growth ETF (IVW). This month, the Value ETF turned 5.7% lower, while the Growth ETF is 8.4% lower on the month. If this pattern holds for the remainder of October is the fourth month for value to outperform growth in 2018. Additionally, although 2019 earnings growth expectations have been reduced from 11.4% in June to 8.1% currently, value expectations have moved higher, with the current estimate pegged at 9.7%, up from 9.3% in June.



According to a Deutsche Bank report, the third quarter saw over $6 billion flow into value ETFs, 24% more than the second quarter; growth funds meanwhile saw a 71% decline in quarter-over-quarter inflows, registering only $1.7 billion in new assets.

With bearish signals beginning to overtake the market and rising interest rates discounting future earnings, it could finally be time for value to sustain outperformance of growth stocks. **Launched August 28, 2015.**

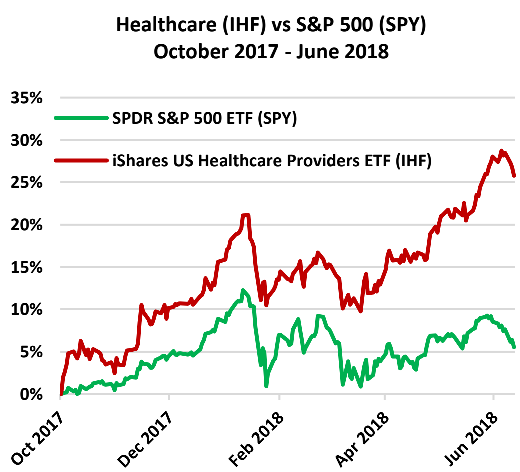
Themes CLOSED Since March:



LONG Homebuilders

After more than 6 years on MRP's list of themes, we chose to pull the housing theme on signs of rising materials costs, rising mortgage rates, and a brewing shortage of homes; many of the same signs that led us to initiate our current short position on the sector.

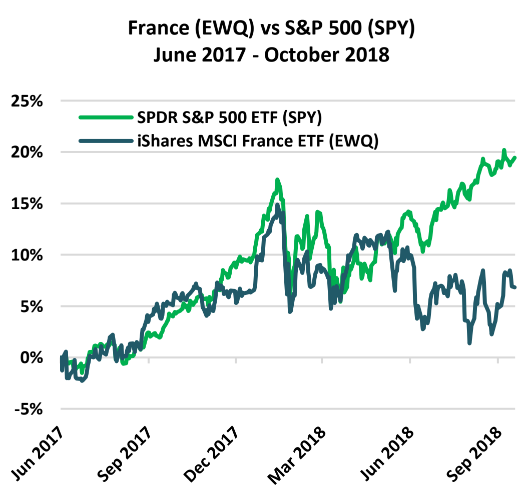
Launched Nov 3, 2011. Closed May 21, 2018.
The S&P Homebuilders ETF (XHB) and iShares Home Construction ETF (ITB) returned 146% and 257%, respectively, versus S&P 500 return of 117% over the same period.



SHORT US Healthcare

MRP's original rationale for shorting the healthcare sector was based on our prediction for the underperformance of hospitals. However, the ETF we chose to represent the sector outperformed due to heavy exposure to medical device companies that garnered strong returns.

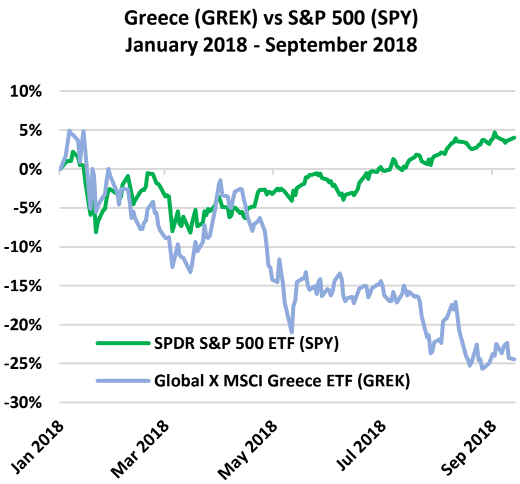
Launched Oct 16, 2017. Closed June 27, 2018.
The iShares US Healthcare Providers ETF (IHF) returned 26% versus the S&P 500's 6% return over the same period.



LONG France

While President Macron had early success, his approval rate has since fallen to just 29%. the country's 9.5% unemployment rate remained amongst the highest in the EU, and September economic growth reached a 21-month low as the French Central Bank trimmed the annual growth forecast to just 1.6% through to 2020.

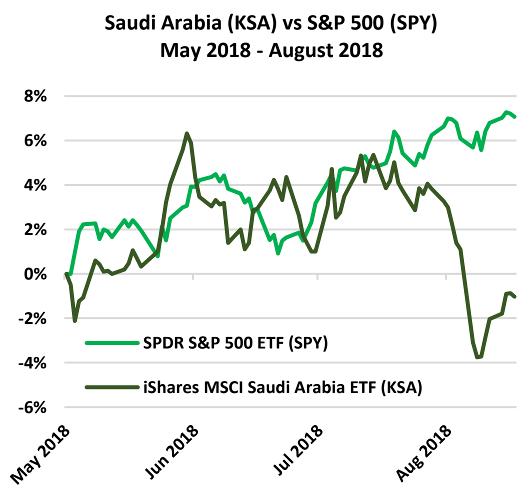
Launched June 14, 2017. Closed October 2, 2018.
Since the theme's launch, the iShares MSCI France ETF (EWQ) has returned about 5% vs the S&P 500's 20% over the same period.



LONG Greece

Greece did exit its bailout plan and has begun to reform its massive slate of non-performing loans, as MRP predicted. However, the country is still reliant upon European Stability Mechanism funds. Greek economic growth also slowed in the second quarter of this year, expanding only 0.2% QoQ, Unemployment also remains at 19.1%.

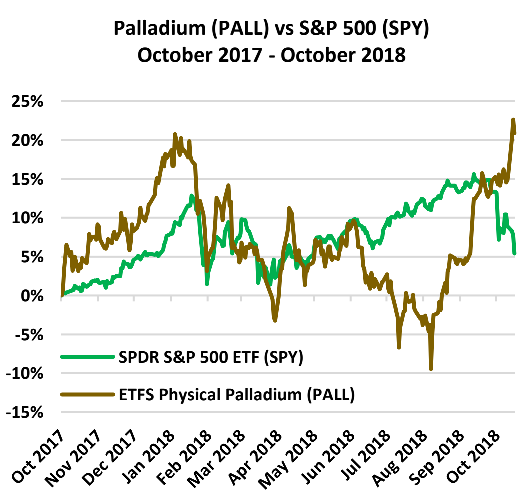
Launched January 19, 2018. Closed September 28, 2018.
The Global X MSCI Greece ETF (GREK) lost about 24% compared to an S&P 500 gain of 2% over the same period.



LONG Saudi Arabia

MRP suspended this theme due to the Kingdom's abrupt decision to cancel the Aramco IPO, as well as the exacerbation of tensions in the middle east from new sanctions on Iran, would disrupt the Saudi Vision 2030 economic reform Plan.

Launched May 7, 2018. Closed August 23, 2018.
The Saudi Arabia ETF (KSA) outperformed the Emerging Markets ETF (EEM) by over 5%, but returned a total loss of 1% versus an S&P 500 gain of 7%.



LONG Palladium:

Palladium is primarily used to scrub emissions from catalytic converters in motor vehicles. While less efficient, platinum can get the job done as well in larger quantities. At this point, the price of platinum and palladium have diverged so strongly that larger quantities of platinum may soon become more cost-effective and begin replacing palladium.

Launched October 9, 2017. Closed October 24, 2018.
The ETFS Physical Palladium ETF returned more than 21%, outperforming the S&P 500's return of only 5%.

The broader market's downturn toward correction territory has had a negative effect on most stock prices and some of our themes have not escaped the carnage. MRP maintains these themes based upon change-driven, fundamental disruptions.

Additionally, this downturn is not totally unforeseen. In the past year, MRP has issued multiple reports elucidating upon numerous risks to equity markets including rising rates and inflation, extended valuations, and the currency translation effect. Only time will tell exactly how far down we could see the S&P dive, but it appears "The Gathering Storm" which we warned of in September 2017, is finally upon us.

Joe Mac

For MRP's research disclaimer, please go to www.mcalindenresearchparters.com/disclaimer.html