

The Outlook: March 11, 2022

Oil: “The world’s turned upside down,” say the speculators. “Probably not,” says Main Street.

Markets are always roller coasters—but the ride we’ve been on for the last few weeks has made the markets’ normal gut-wrenching behavior seem like a rowboat ride on a placid pond. Oil, wheat, copper, steel, common stocks and nearly everything else have been plunging up and down as if they reflected a world in which all rules were off: “the world turned upside down,” like the tune played by the British Army surrendering at Yorktown.

The wild plunges, of course, do not reflect a real world in which “all rules are suspended.” They simply reflect the giant professional betting crowd trying during every passing hour either to make money or avoid losing their shirts. The events happening in the real world (“Main Street”) are emphatically more startling than usual . . . and the betting crowd’s reaction is to run wild in both directions—sometimes on the same day—as it tries to cope with this situation. Speculators drive all financial markets in the short run; and they always exaggerate the direction, either up or down. That’s just what they’re doing now, but in spades.

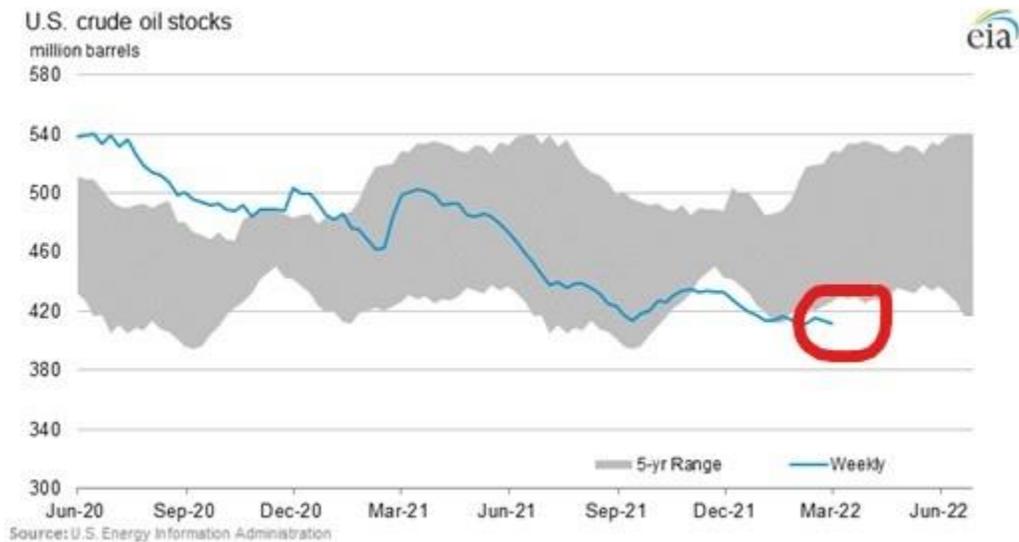
To see this a little more clearly, let’s glance at one different corner on Main Street—oil—which has been grabbing headlines lately. Here’s Conoco and oil prices.



The yellow arrow is West Texas Intermediate, going literally “off the charts.” Purple is good old Conoco, rising strongly since late 2020, and sharply since oil’s latest “off the charts” moments. As oil rockets up and down, and Conoco rockets with it (but at a calmer pace) the obvious thing to wonder about is: “How

high can that yellow arrow go? Is it already so stratospherically detached from Main Street that we should sell Conoco?"

Outlook's answer is: "It's somewhat detached, all right, because the betting mob has no idea at all where real-world supply demand for oil will set its price, when the real world has calmed down. But Conoco is another story. It's not the slightest bit detached from Main Street reality, at today's stock price. Because of its tremendous hard work over the past few years, Conoco will be creating a river of cash flow and earnings for years to come, at any oil prices between \$60 and \$120." And where in that big range might oil finally rest, for a while? Here might be the one picture which sums up what's been happening with supply and demand on Main Street:



The gray shade is the range for U.S. oil inventories since 2017. The thin blue line is U.S. oil stocks at the moment. Those stocks were far above historical norms in mid-2020. Now they're below the bottom of that 5-year range. It took a long time and lot of steady changes in demand and supply for that to happen. It won't be reversing course anytime soon. Today's oil at \$115, or tomorrow's at \$130 or \$100, don't matter much. What matters are the long years of cost-cutting (bringing Conoco's break even oil price from about \$60 to about \$30) and the irresistible return of global oil demand, after the short-lived shock of the Virus and Lockdown Calamity. Conoco will be benefiting from both for a good while, no matter what kind of rockets the speculating crowd rides from day to day over the next weeks and months.

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Outlook Capital Management, LLC
125 S. Wilke Road, Suite 200E
Arlington Heights, IL 60005
847-797-0600

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