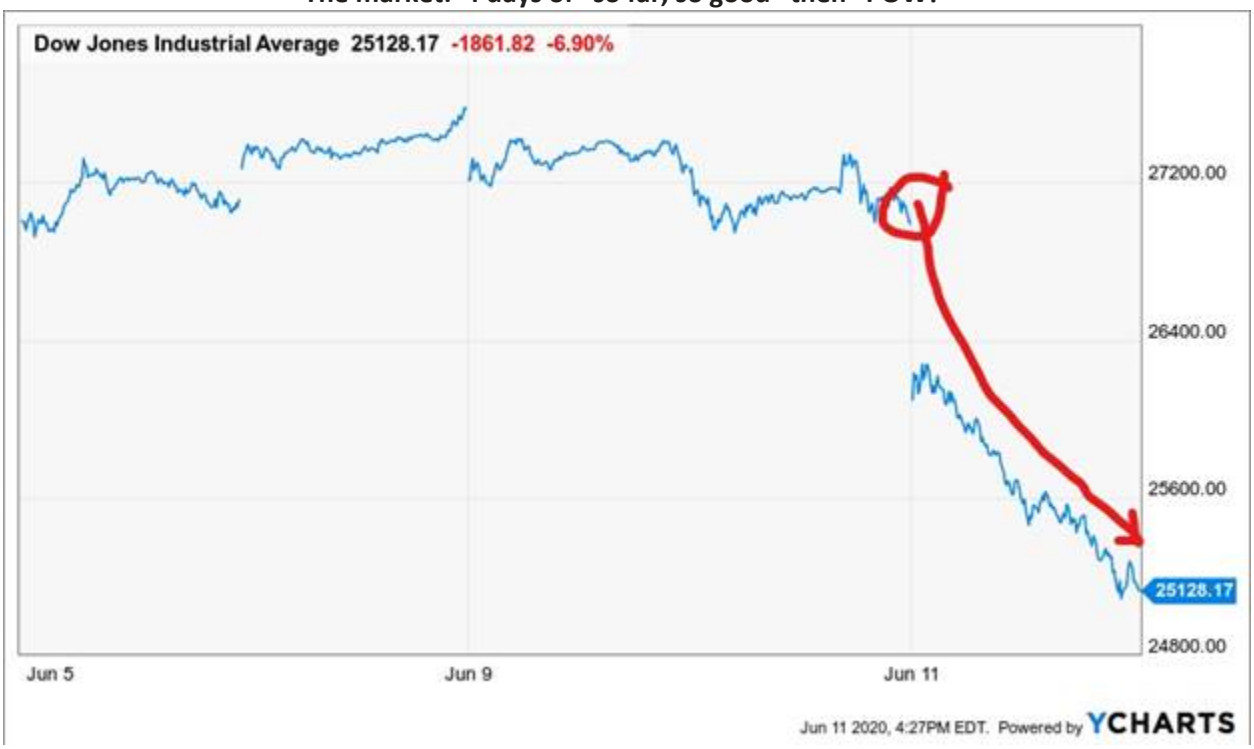
The Outlook: June 11, 2020

Taking educational lumps, today.

If indeed "we learn more from taking lumps than getting gifts," then today was a very educational day. Down plunged the market by 1,861 points, which was probably a big enough lump to shake the newborn confidence of the cheeriest optimist. It's back to cold compresses and aspirin for a while, we all feel, and just when the first faint thoughts of champagne had been bubbling up (along with the 40% rally since the depths of March.) Here's how it looked.

The market: 4 days of "so far, so good" then "POW!"



As always, here's the Big Question: "Did today's "POW!" tell us something profound? Did it warn us the faint stirrings of optimism built up since March were delusional, and we should have listened to those voices calling out warnings about the Ides of March, don't go to the Forum, dig a hole in the back yard for your cash, etc."

Or did it mean nothing much . . . just the speculating mob acting in character?

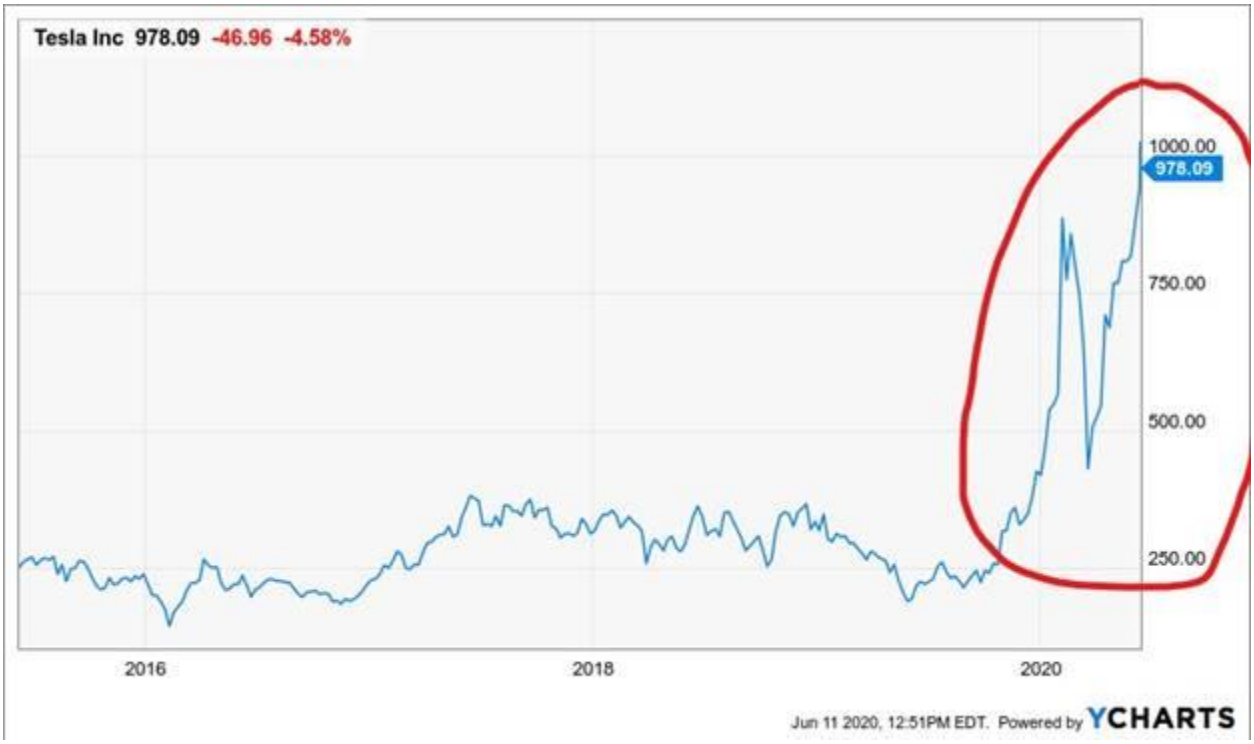
That gave away Outlook's answer, of course. But it *was* an educational day. Let's find out why—by glancing at some charts which look like they've got nothing to do with it.

Chesapeake Energy Trembling on the Verge of Bankruptcy, This Week

Chesapeake was the original Shale Fracking King, pretty much. It is the story of the U.S. shale boom: daring land buys, innovative technology, go-for-broke cowboy capitalists in charge . . . who ran into a law of geophysics called "decline rates," which mean that shale wells begin with gushers, but slow down to trickles with sickening speed. To offset that slowdown, Shale Kings like Chesapeake had to constantly spend gushers of money on both new and existing wells. They borrowed most of it, which is the same thing as saying they signed their own death warrants, with dates to be filled in at some inconvenient time in the future. 2020 is the date. Chesapeake has been teetering on the edge of its certain bankruptcy filing for months. There will be no money for its stockholders, whenever it decides to stop teetering. Yes . . those common shares will be worth zero. Hence the education, above. $17, 5 days ago. $85, 3 days ago. $17, today . . . $0, quite soon.

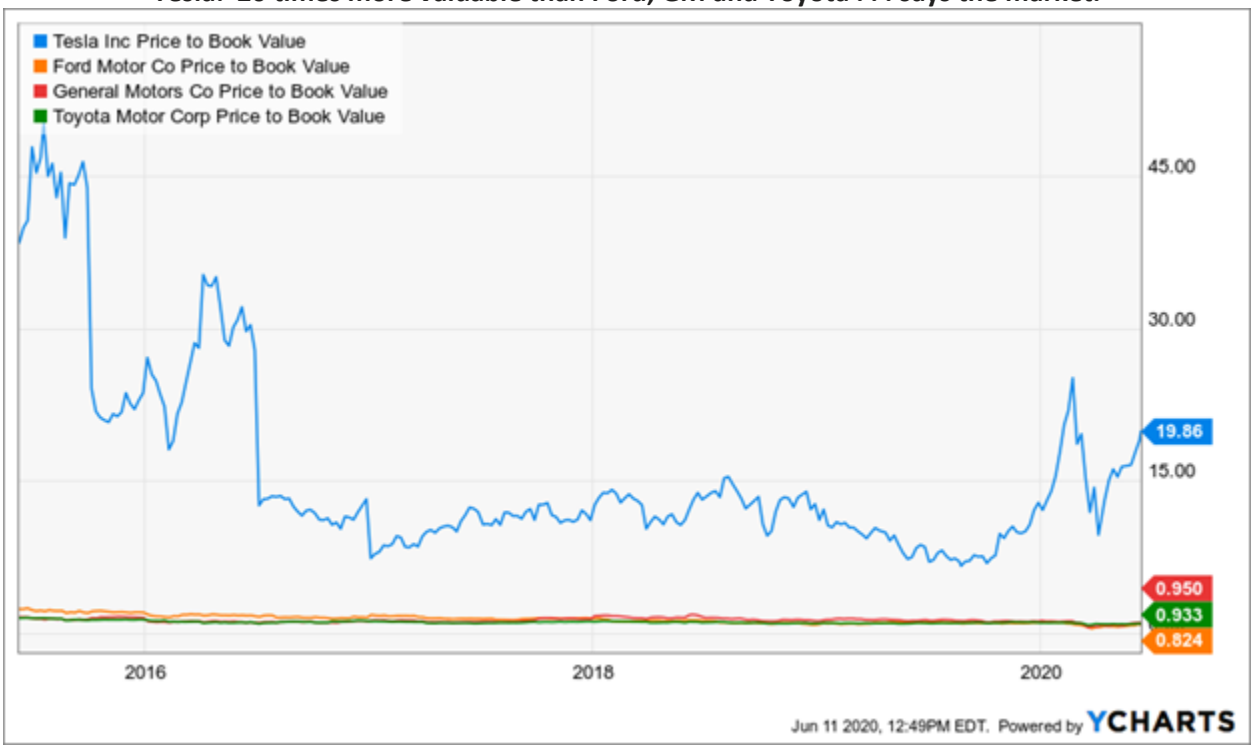
There are many guesses about "who" has been ignoring the laws of nature, geophysics, accounting and bankruptcy while buying and selling Chesapeake shares lately. The favorite guess is "Millennial nut cases trading on Robinhood" (a zero-commission internet trading platform for, well, millennials among others.) No doubt that's part of the answer, but at Outlook we suspect that when the dust clears we'll see the foolishness was shared far and wide through the speculating crowd: from "sophisticated" hedge funds to day-trading computer jockeys. But whether they're hedge-fund billionaires or day-trading young men, most of them probably know Chesapeake is worthless. The company's 2-month bonds traded today at 6 cents on the dollar for a yield of 6,700%, which is slightly more than a subtle clue. (More like a neon sign blaring "Worthless!") No . . . the gamblers who drove Chesapeake from $17 to $85 a couple of days ago were buying for one reason: <u>because everyone else was buying</u>. Let's glance at a different picture.

Tesla, 5 Years



In 8 months or so, Tesla has risen from $250 to $1,000 per share, all in that red circle. Here's our Big Question, again: "Is that telling us something profound . . . or is it just the market (the speculating mob) acting in character?" We need another couple of charts.

Tesla: 20 times more valuable than Ford, GM and Toyota . . . says the market.

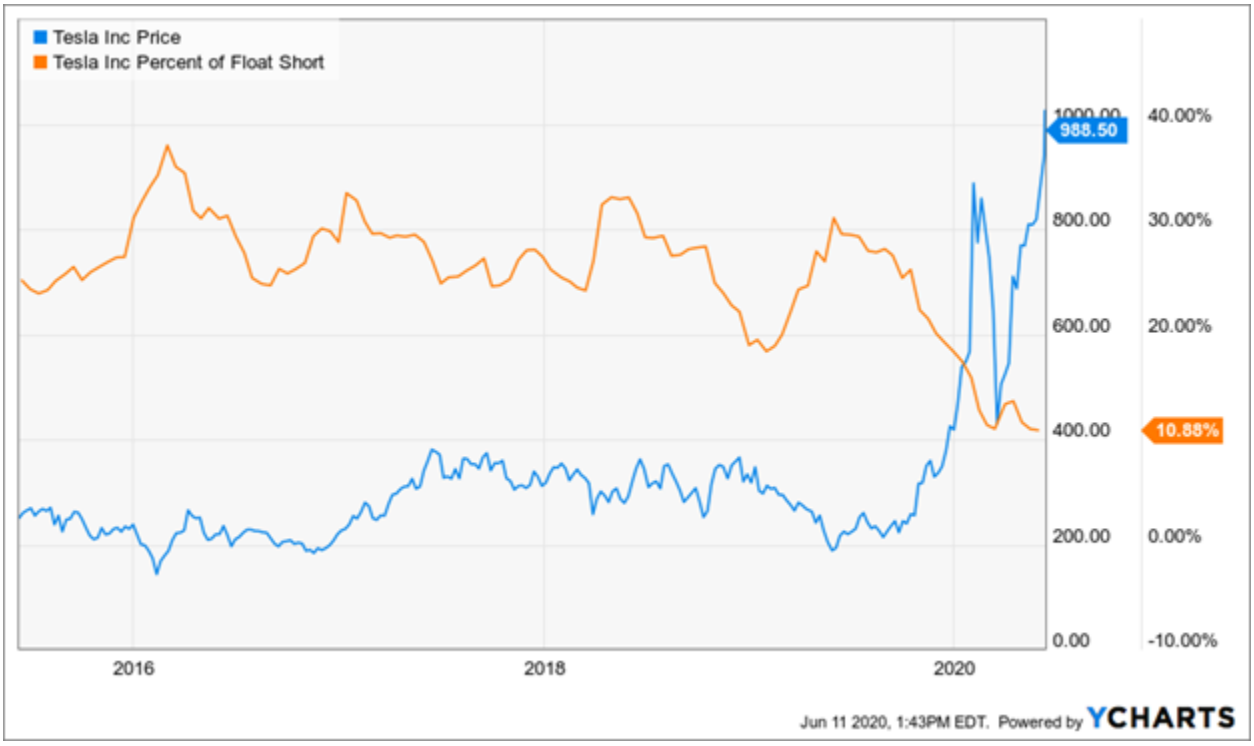


Tesla was 50 times more valuable than Ford, GM and Toyota a few years ago, the chart tells us—so perhaps the speculating mob has acquired wisdom and restraint with the passing years. (Perhaps we won't bet on that.) But perhaps Tesla has become profitable lately? Perhaps not: here's that picture.

Basic EPS (Annual)	2019-12	2018-12	2017-12	2016-12	2015-12	2014-12
EPS Basic from Continuing Operations	-4.92	-5.72	-11.83	-4.68	-6.93	-2.36
Normalized Basic EPS	-4.221	-4.978	-11.83	-4.68	-6.93	-2.36
EPS Basic	**-4.92**	**-5.72**	**-11.83**	**-4.68**	**-6.93**	**-2.36**

Here's the last picture: the most educational of all (and probably the most satisfying to Mr. Musk, who is certainly one determined and daring individual.)

A 5-year lesson for the speculating crowd: "the market can stay irrational longer than you can stay solvent."



The orange line is the percent of Tesla's tradable shares sold short by speculators willing to bet their sacred fortunes (or part of them) that Tesla is a high-wire act without a safety net, and the next big wind will blow down the whole circus tent. Notice the end of this story at the far right: after years of 30% short bets against the company . . . those bets have plunged to 10%. Either those gamblers have finally run out of money, or they've given up and wandered off to get in on the action in the frozen orange juice pit, with the Duke brothers.

What do these pictures have in common with the Dow's death plunge, today?

Yes, they're all pictures of the market's speculating crowd acting normally. That crowd makes its living by trying to "get in on the action," up or down. Most of the time, the "action" is pretty confusing, and not very persuasive in either direction. But every once in a while, an impression created by the daily news seems pretty powerful. (Meaning, it sounds like it'll persuade most of the crowd to act the same way for a day, week, or month or so.) That means "action" worth betting on for a day, week or month . . . with one eye cocked at the Exit door at all times.

If we investors—or all those speculators—ever bothered to look back, later, and think about the exact news items which made strong impressions on the market . . . we would shake our heads in disbelief most of the time. Today it was, "Fed Chairman Predicts Long, Slow Recovery!" plus "Virus Cases Surge, in Some Places!" Of course the Fed's history of accurate forecasts is as awful as everyone else's; and of course buried under the "Virus Surge!" headline was "Total U.S. cases rise less than 1%, smallest since March." But the market crowd acts upon impressions. Thankfully for long-term investors, the endless stream of real facts constantly sets boundaries on just how far and long the market can act on impressions which aren't supported by facts. It will be doing that again, probably in the near future . . . unless our political leaders seize upon "Virus Cases Surge!" to start another Shutdown Calamity. (That nightmare was surely what the market crowd was really reacting to, today.) Some of them might try it, politicians being what they are . . . but that kind of Nightmare just won't work as well the second time around, on most people.

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