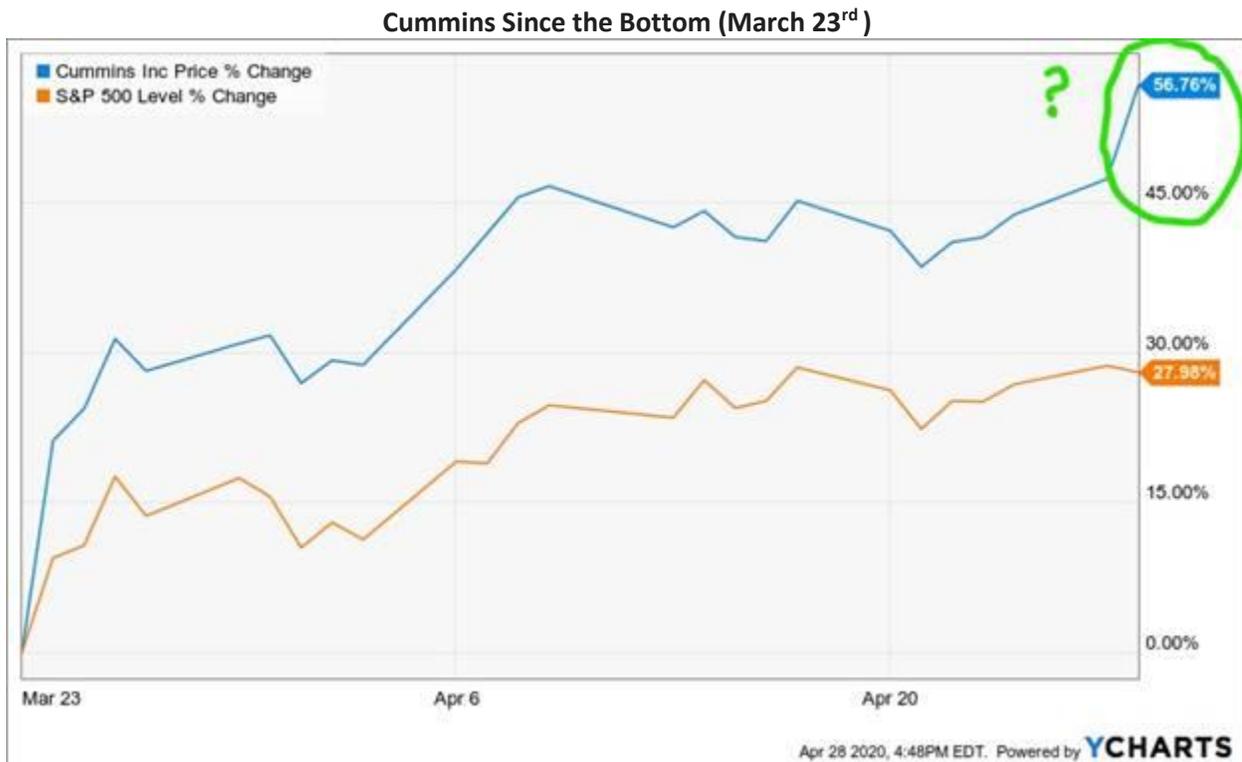


The Outlook: April 28, 2020

“Not the slightest idea” about 2020 . . . but Cummins does know its future.

This picture captures the heart of the “Big Questions” about a lot of things, today:

- Why on earth has the market done so well since the abysmal March 23rd bottom?
- How on earth did a heavy industrial company like Cummins (the Diesel Engine King) not only do so much better than the market since that bottom, but also pop 6% today, after an earnings report in which the company said, “We don’t have the slightest idea what will happen this year”?



“We don’t have the slightest idea!” is everyone’s favorite sentence these days: from CEO’s to economists to investors and even politicians. The CEO’s are talking about the future—the rest of 2020—when they use that sentence. They have a rock-solid understanding of what has happened to their companies up to this moment; and for most of them, it’s been like getting clobbered with a rock. The Global Virus Shutdown hammered sales and cash flows harder than anything they’d seen since 2008 . . . and sometimes even harder. They knew it would happen, and they know the second quarter will be a lot worse. And finally, they don’t know when it will get better. “We don’t have the slightest idea!” indeed. But there’s the market, up 28% from that bottom; and there’s Cummins, up 57%.

Why?

There are 2 possible answers. The one we investors choose will depend on some very fundamental things about ourselves and our understanding of “how the world works.”

1. **“The market is delusional. The March crash was just a warmup. The next one will show that “misplaced optimism” is deadlier than the Virus, for investors.”**

This answer rests upon a basic fact and a basic risk. Neither is the slightest bit imaginary. They’re very real. The basic fact is that this economic and market meltdown is something new in history: the deliberate act of political leaders around the world. The basic risk is the other side of that coin: those political leaders have to act, again, to give the meltdown any hope of reversing itself . . . and they have to “get it right” for that reversal to be permanent and strong.

In the long run, all economic growth, individual well-being and wealth creation are at the mercy of political leaders. Those leaders never create the growth and wealth . . . but they can cancel it out or drag it down, when they do the wrong things.

They “do the wrong things” often enough to worry anyone. All by itself, that statement sums up the strength of “Answer Number One.” Let’s look at Answer Number Two.

2. **“The market is not delusional—at the moment, anyway. It certainly was on March 23rd, when it reached levels suitable to a global famine, meteor strike or world war . . . but not suitable to a reversible political decision. The market’s happy behavior since then hasn’t been “happy” at all, but simply a recognition that “sky is falling” values can’t be sustained when the sky actually isn’t falling—even if it has created economic hurricanes, tsunamis and flash floods from New York to New Delhi.**

Answer Number Two is the right choice, of course. In every single Calamity from the Depression through the Panic of 2008, the market has behaved in exactly this way: first overdoing it, throwing assets into the garbage to lighten itself up, so it can run for the hills before the sky actually crushes everything; then admitting the sky appeared to be still up there among the clouds, and maybe stock values had crossed the line into insanity, and ought to be picked back up from the garbage dump. But there is more for us to think about, beyond understanding that Answer Number Two is a sound explanation of the past month.

That’s where Cummins comes in . . . and that green circle around today’s 6% pop.

CEO Tom Linebarger, this morning, sounded exactly like Freeport’s Richard Adkerson the other day, and like Caterpillar’s Jim Umpleby (also this morning) . . . and like very many American CEO’s are sounding this Earnings Season.

- “We absolutely can’t tell you how this year will turn out. We’re all just guessing about how soon and how strongly the world economy might recover, and our customers might start buying again.”
- “But we can tell you what we’ve done to handle this problem. We began with excellent cash and financial strength, and we’ve already greatly increased them. We acted instantly, pretty much, to lower our costs and cut any risks; but we refused to take any action which would cripple Cummins’ ability to rebuild earnings and cash flows (and shareholder rewards) very strongly in the future.”
- “Finally, here is what we’re seeing right now. 75% or more of our global plants are operating right now. They’re all working at slower paces . . . but they are operating. There has been a startling surge in demand for Cummins’ products in China (from Chinese truck makers and users of backup

power generators.) We are sure that kind of strength in demand is temporary to some degree, reflecting the first weeks of “back to work” operations among our Chinese customers. But even so, it’s been much stronger than the slow, cautious return we thought we might have seen. China is absolutely ahead of the rest of our worldwide markets in this “recovery timeline,” but there are distinct hints that we might see the same thing in the rest of the world, with a lag.”

And that was the heart of what Mr. Linebarger had to say, beyond the usual wealth of details about Cummins’ operations. “We’re stronger than ever. We don’t know how long we’ll need to endure this. We will come out of it with a bigger lead over our competitors than ever, because we have the strength to keep investing for the future.”

To investors with a deep belief in the power of outstanding companies and their people to fix any problem and return to strong growth, that would always be worth today’s little rocket ride. The crowd of speculators who dominate the daily market don’t often seem to care much about that kind of belief. But they’re forced to care about it, when the valuations of great companies are still down there somewhere close to the bottom of the cliff. At Outlook we think Mr. Linebarger’s facts about his company’s strength were only slightly surprising to that crowd, this morning; but they were enough to remind the crowd that Cummins’ sky is very far overhead indeed, and not remotely likely to fall.

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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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