

The Outlook: June 12, 2024

Caterpillar reminds us of the nature of the market . . . and what's worth betting on.

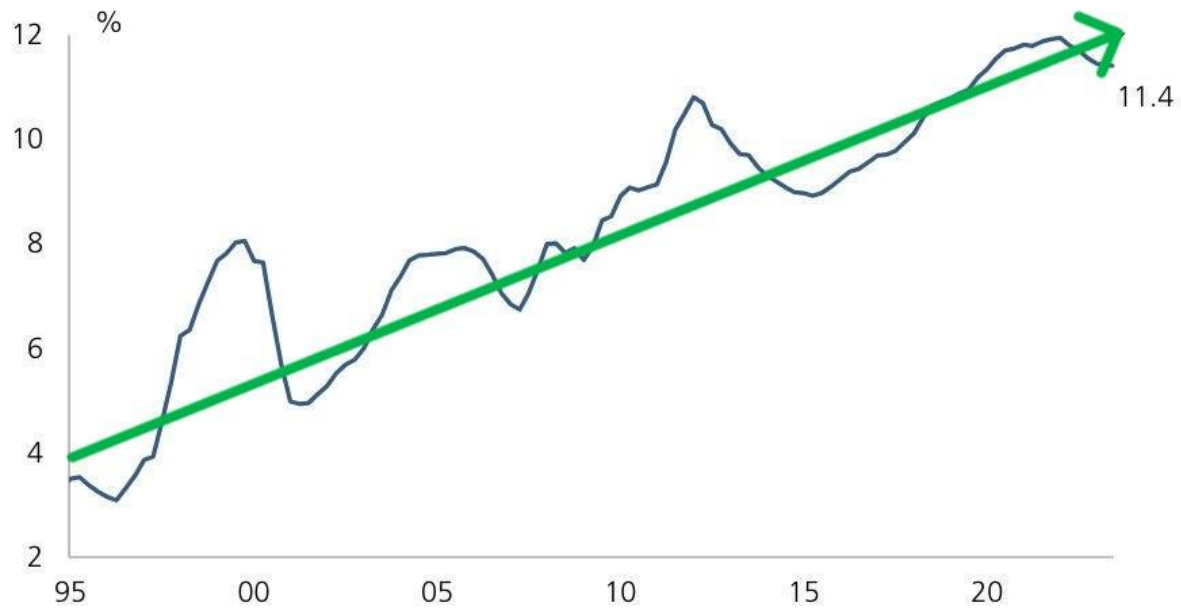
We do repeat ourselves a lot, when it comes to a handful of “very important” subjects. They’re so crucial for our investing success that we just have to keep at them. One of those subjects is: “Understanding the nature of the market” . . . so here we go again.

The “market” is driven every hour and day by a truly vast crowd of speculators: from clueless young men trying to strike it rich on the “Robinhood” market site, to giant hedge funds and other professionals using nano-second trading techniques and higher mathematics. But the clueless guys and the sophisticated algorithmic traders—and the huge crowd in between—are all essentially doing the same thing. They’re betting money based on the impressions created by the daily headlines—for a few minutes, hours or days—to make a quick killing. Betting being what it is, somebody certainly gets “killed” as a result, quite often the gamblers themselves . . . but it’s amazing how we almost never hear about that body count.

The key word in all that was “impressions.” Being normal people, the giant betting crowd very often makes decisions based on “impressions” rather than long, slow digging for information and understanding. And around 99% of “impressions” are misleading, distorted or downright wrong—especially the impressions handed us every day by the media. Now, all that makes it sound as if we’d be nuts to have anything to do with the market ourselves . . . except for one thing: in addition to betting on all those impressions, the market gambling crowd must also bet on the truth when it comes along; on cold hard facts about how Main Street’s companies are actually performing . . . and especially about the cold, hard cash those companies are earning and giving back to their investors. Time for some pictures.

Miracle on Main Street

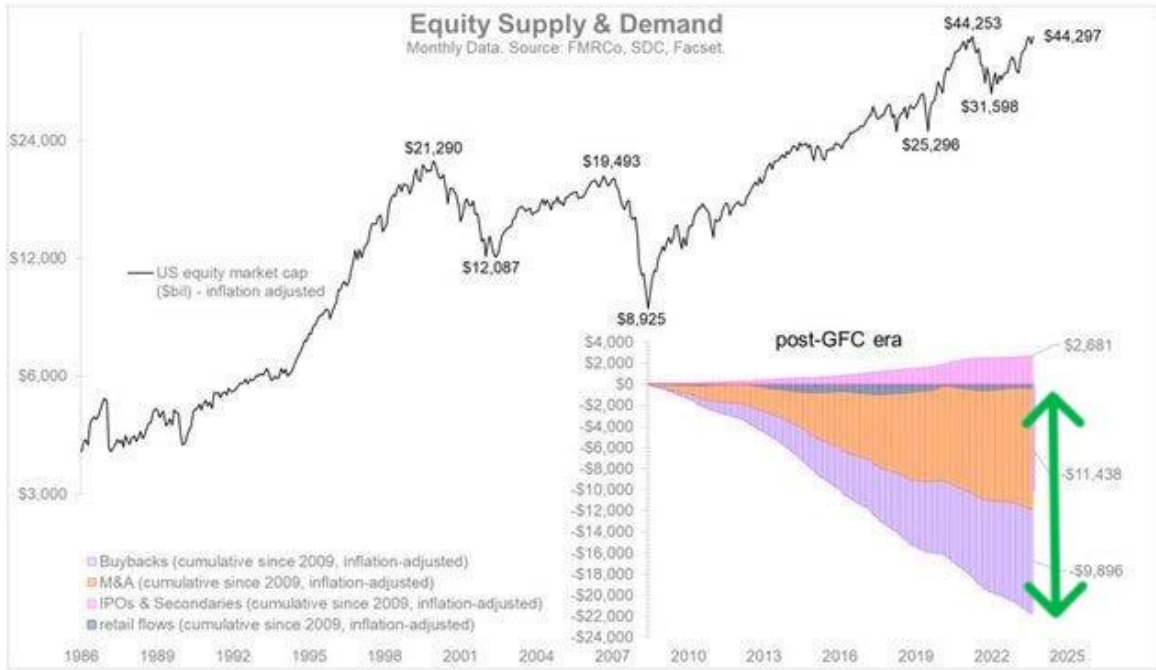
Figure 7: Free Cash Flow as a % of Sales - S&P 500



Source: Standard & Poor's, FactSet, UBS
Note: Trailing 12-months, 4Q Moving Average, excludes Financials and REITs

The best title for this chart really is "Miracle on Main Street." 30 years ago Big Corporate America converted less than 4% of every sales dollar into "free cash flow" available to reward its patient investors. Today it converts 11.4%. That's the story of managements making their companies stronger and more profitable decade after decade . . . which is what they're paid to do. This next picture is way too complex, so our title tells the story.

Green Arrow: Since 2009, \$3 Trillion of New Shares Issued . . . \$21 Trillion of Old Shares Bought Back and Eliminated

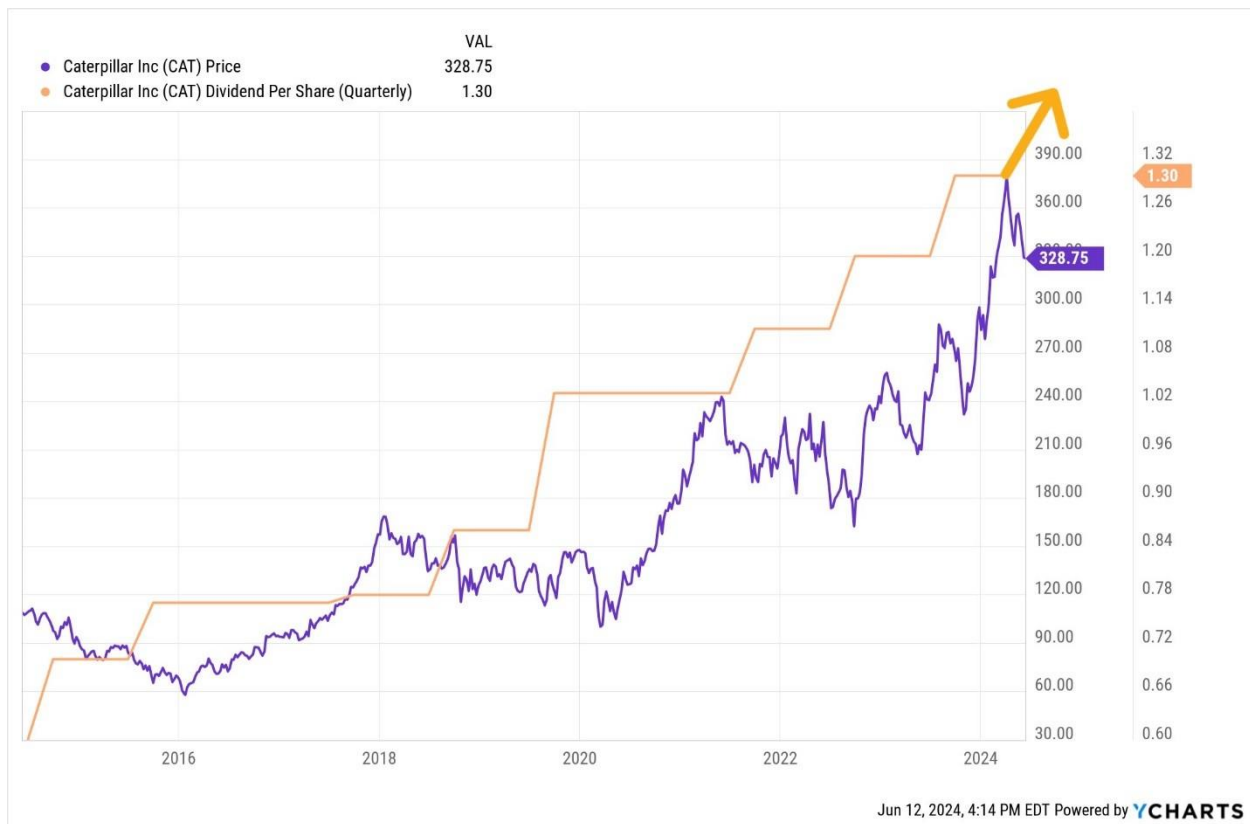


Data source: FMRCo, Bloomberg, Haver Analytics, FactSet. Data as of 06/02/2024. Past performance is no guarantee of future results.



When one of our companies buys back its own shares, remember, it gives each of our shares a bigger claim on the company's assets, earnings, cash flows and dividends. When our companies send us dividend checks, it's an immediate pleasure . . . but when they buy back shares, we don't get the instant reward . . . but we do get the certainty of bigger payoffs down the line, just like an investor whose 1% ownership stake was converted into a 5% ownership stake as a gift from the company. Last picture.

Caterpillar: Today's 8% dividend hike . . . and all the others, for 10 years.



Caterpillar’s 8% dividend hike, today, was the result of our first two pictures: management doing a remarkable job of strengthening the company—year after year and decade after decade—creating exactly the kind of facts about “cold, hard cash” which the market’s betting crowd must respect and must bet on, when those facts show up in between the barrage of silly impressions which usually drives the crowd’s decisions. That steep, long-climbing purple line up there is Caterpillar’s stock price. It’s risen 450% since 2016 because of those cold, hard facts about cash . . . not because of the endless silly impressions floating past us every day. That’s something worth betting on.

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