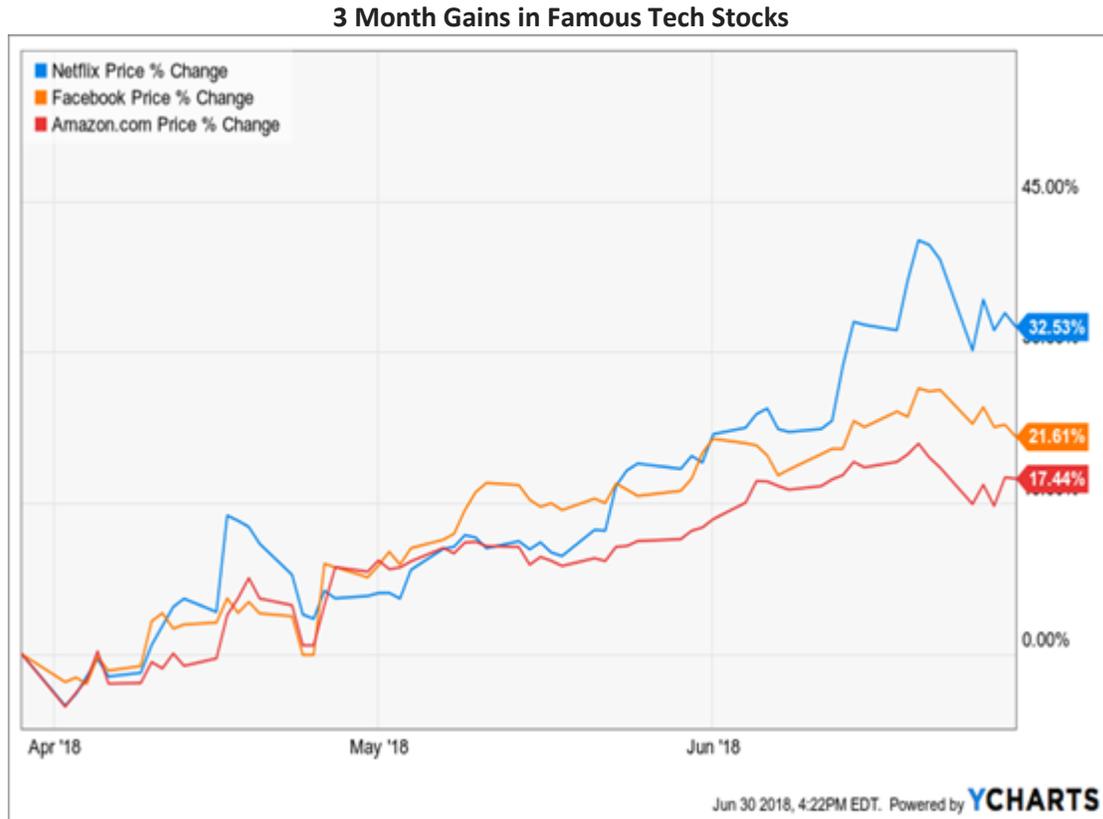


The Outlook: July 1, 2018

Stepping back: what's going on in this market?

“Tech Stocks Shine in Rocky Quarter!” was the headline, next to a truly spectacular chart somewhat like this:



If we value our sacred fortunes, we investors must step back, pretty often, and ask: “What is going on in today’s stock market? What’s the heart of it? Are we in big trouble, or not?”

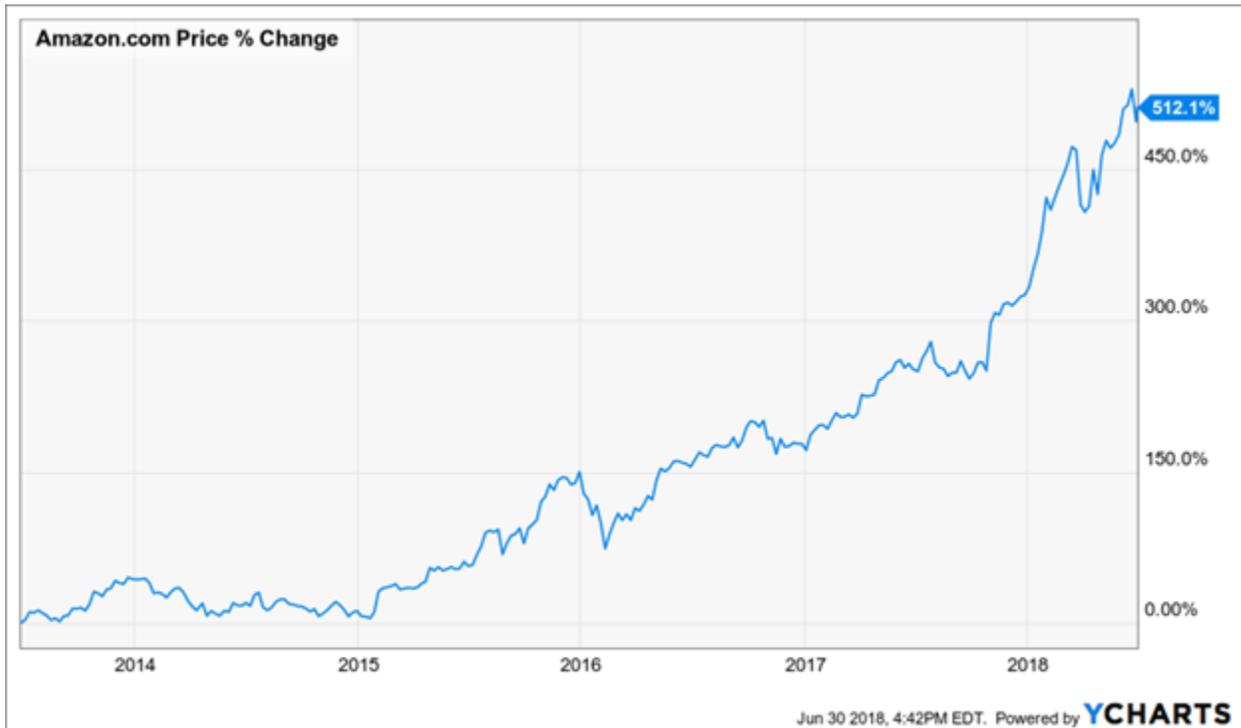
That headline and that chart must trigger some sharply different feelings among investors. For those (unlike Outlook) who’ve owned Amazon, Facebook or Netflix there is sheer delight, plus for some of them, surely, the sense of danger that comes to most investors who’ve been around the block a few times, and experienced the downside of the roller coaster. For everyone else there’s surely some mix of feelings ranging from “Is it too late to get in?” to “Those people are nuts!” No matter which group we’re in, though, we must decide what our opinion is about these Tech Rockets, because it’s half the answer to our “What’s going on today?” question.

Let’s zoom in, looking only at Amazon—whose size, strength and real achievements certainly make it the most “solid” of those three Tech Rockets. Our question will be, “Yes . . . but how solid?”

Amazon: One Year Gain



Amazon: Five Year Gain



Those two charts picture a company which has achieved astounding things. They also picture a stock trading at 85 times earnings, while the market trades at 17 or so. And they picture a company which is acting, now, as if it thinks it can dominate any industry it chooses to enter. Finally, they picture a market which acts as if no reasonable person could doubt that Amazon will always win those battles. The latest

example of all this is last week's \$1 billion purchase of a tiny drug-supply company named PillPack, by which Amazon announced that the drug-supply industry is next on its "Dominate" list. The day of the announcement, the 8 or 10 experienced giants of that industry—all haystacks to PillPack's needle—plunged 5% to 10% in price, courtesy of the market's opinion that we mustn't doubt the belief that "Amazon always wins."

Here's Outlook's opinion. "Amazon always wins," is precisely the kind of silliness which we nearly always see when the stock market is poised at the edge of a cliff, ready and willing to nosedive like Wile E. Coyote to a puff of dust far below. And in fact, it's precisely the kind of shallow-thinking optimism—we might say—which we human beings usually tend to attach to "celebrated superstars" in most walks of life. It often seems, for a time, as if they can do anything. It never turns out that way, even if they actually are mighty impressive people.

So that's Amazon: the truly solid member of that "Tech Rocket" club. (We won't explore Netflix and Facebook. It would be altogether too frightening.) Is that the heart of the market, today?

Nope. Let's look at the other extreme.



Not far from Amazon's neighborhood this past year, is it? But even the picture alone shouts at some differences. Micron's delightful year has given investors ulcers. We can see those sharp points and awful plunges up there, and remember the sickening feelings in the pits of our stomachs, as we reached again and again for the Alka Seltzer. That's trivial next to the next difference: Micron trades at 5 times earnings. Yes, five. The market's opinion of this company, and its stock, appears to be etched in concrete: namely, "Just wait, the bottom will be falling out tomorrow, or maybe next week." No matter what the company and its leaders have done to build Micron's future, and its financial strength—and their

achievements aren't all that far from Amazon's, relative to the obstacles faced—the market's opinion is unchanged. "Five times earnings for this stock, because it'll be a puff of dust down below, pretty soon."

The silly thing about this market opinion—not as silly as the "Amazon Always Wins" notion, but in the same ballpark—is that at 5 times earnings, Micron stock is already valued as if it's the puff of dust down there. When bad news comes, exactly where is there left to go (in the downward direction) for a stock which is valued, today, as if the cliff-dive in the company's operating performance has already happened?

One answer, of course, is that the market is always capable of going from "silly" to "insane" when it comes to any stock, in either the up or down direction . . . for a while. But the difference between the market and a casino is that real facts and real achievements rule, in the end, for the economy and for any company and its stock. The roulette wheel always rules in the casino. Earnings, dividends, cash flow and business growth always eventually rule the market—not the other way around.

"What is going on?" in today's market is a striking mixture of silly optimism attached to relatively few big companies, mostly "Celebrity Tech;" and very stubborn, deep-rooted pessimism (or at least caution) attached to far more companies. Micron is an extreme example of that, but a great many other strong, industrial companies clearly fall into the "cautious to pessimistic" market opinion, rather than anything approaching unguarded optimism.

So "What is going on," is somewhat peculiar, when we consider these extremes of opposite attitudes. Peculiar, odd . . . and in the nature of the market, pretty often. Those Tech Rockets are riding for a fall, someday. There's no room in their valuations for anything except astonishing success, continued indefinitely. For any investor old enough to have a few scars, those words are somewhat terrifying. But at the opposite end, starting with Micron and extending to companies like Caterpillar, Cummins, Conoco, Freeport, Shell and many others, there is little room in their valuations for more damage, if the bad news the market expects for them ever actually arrives. An odd market, indeed. Fortunately, the people within such companies who make the future happen aren't paying attention to the market's peculiar attitudes. They are building and strengthening foundations which are already remarkably strong; finding alternatives and solutions to threats ("Trade War" being near the top of the lists, no doubt); and knowing that the market—since in the end it's absolutely not a casino—must recognize and properly value what they've accomplished. At Outlook we believe one of the best possible attitudes for investors is exactly the same attitude shared by the people who lead and work within the companies we own.

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