

## ***Inside Caterpillar: Last Quarter's Progress.***

***Oct. 29, 2020***

At first glance Caterpillar's last quarter was pretty terrible across the board, with sales down 20% to 25% from a year ago in every division. A second glance shows sales up a tiny bit from 2020's calamitous second quarter (in the middle of the first lockdowns), which is good news in the same way a sprained ankle is better than a broken ankle. When it comes to real recovery from the worldwide economic plunge caused by the lockdowns, Caterpillar is definitely still looking for those first "green shoots" to show up, rather than celebrating the V-shaped rebounds seen in other kinds of businesses.

China is one of them, for Caterpillar; and strong preliminary buying interest from mining companies is another. A third is residential housing construction. There will be more green shoots—but Caterpillar would not make any guesses about exactly when. ("Eliminating forward guidance" is the term.)

We always believe we can understand a lot about a company when it's under great stress. Despite the sales weakness, CAT had a more profitable quarter, reporting an operating margin of 10% versus 7.8% three months ago. Controlled costs, increased factory efficiency, and a favorable geographic mix of sales all helped its bottom line. Here was the best part: Caterpillar produced \$900 million in free cash flow, almost double last quarter's \$500 million.

As a company whose sales typically line up with global economic health, Caterpillar is very used to managing tough times. That increase in profitability and cash flow is proof of this. It is also a financial rock, with almost \$10 billion of cash on its balance sheet, higher than its end of 2019 position. It used \$400 million of this cash to buy Weir Oil and Gas, a company that focuses on pressure pumping and pressure control products for the oil industry. Caterpillar believes that combining these products with its engines and transmissions will increase its value for those customers. CAT is buying Weir "at the bottom" and this action will make our company one of the broadest oilfield service companies in the world.

Here is Caterpillar's stock price since the pandemic's March bottom: up 65% *despite* falling revenues the past 6 months. Caterpillar is not a mystery to the market. It knows that whenever the world's upcycle in industrial spending does happen, CAT will be stronger and more profitable than ever.

Caterpillar Inc Price % Change

