

The Outlook: Dec. 14, 2017

*Freeport in the jungle: copper and political*

Freeport-McMoRan: 3 Years, stock price and cash flow



We've remarked in the past that while every company plunges, sooner or later, into its own personal Valley of Hell—which tests the grit and judgment of all of its people, but especially its CEO—copper king Freeport-McMoRan might deserve the gold medal for sheer depth into the inferno. Our company must deal not only with an eternal, jet-boostered, cyclical roller coaster ride in its flagship commodity, copper; but must also deal with politicians in remote parts of the world, who care nothing for property rights and the sanctity of contracts.

Freeport mines copper (and gold) all over the world, but its own flagship asset is the famous Grasberg Mine in Papua New Guinea—part of Indonesia. This incredibly sophisticated operation sits on top of a 15,000-foot mountain surrounded by jungle, and its ore is so rich that Freeport's cost of producing copper, at Grasberg, is among the lowest in the world. Freeport has been at this project for decades, working with all kinds of Indonesian governments and politicians, and displaying an admirable degree of calm poise and patient diplomacy in the face of what we might politely call "disrespect" for agreements and contracts, especially from the current coalition government. That government has clearly been tempted to just expropriate (diplomacy's polite term for "take") the Grasberg Mine, these past couple of years . . . but has been concerned enough about its international business reputation to stop short of that move.

When the threats began, a couple of years ago, Freeport was not in good shape to fight back. It had bought an oil exploration company at the top of the 2014 cycle, adding much debt at the worst time. (That happens a lot, even to the best of companies and leaders.) In the orange line above, we can see Freeport's operating cash flow plunging, side by side with the stock itself. But CEO Richard Adkerson and his team have been riding the copper roller coaster, and operating in the real and political jungles of "developing" countries, for a long time. They did not sit still, down in the Valley. Like Conoco and Shell,

Freeport sold good assets to raise cash; cut capital spending and costs where the cuts wouldn't cripple its future; and used the cash to rapidly pay off debt. Here's the result through last quarter:



That 50% cut in net debt was the picture on September 30<sup>th</sup>. Within the past month, Freeport has paid off another \$2 billion in debt, using the strongly rising cash flow pictured in that orange line up top. This company is not very far from having its annual cash flows able to cover all of its net debt. And that, in turn, makes Freeport a much stronger negotiator with Indonesia, as they take step by torturous step to inch toward an acceptable compromise contract for the future.

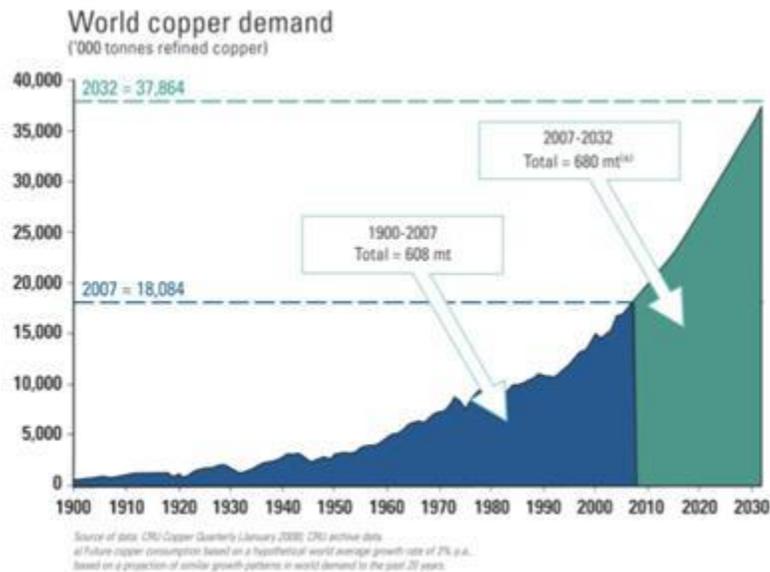
And so it was with real interest, yesterday, that Outlook noticed the news item pictured below:



The man under arrest is a high-ranking official in the Indonesian government, charged by his own government with corruption. Earlier this year a top Freeport manager in Indonesia actually filmed the same politician asking the manager for free shares in the company, in exchange for “assisting” the resolution of the 2-year contract dispute . . . but the video evidence didn’t impress a local court enough to sustain the charges. This week’s charges are not connected with Freeport, and are on a galactic scale by comparison with the video incident.

Politics is funny everywhere, and Indonesia is surely no exception. Freeport stock has been rocketing up lately. While copper prices have been acting lively, which always helps, we might wonder whether the arrest could actually help Freeport and Indonesia to move forward. As the company—and many analysts—have been saying for 2 years now, a mutually agreeable contract is clearly the best outcome for both sides. And squarely under the “politics is funny” heading, came this morning’s news that the company and the government had moved another step closer to reaching agreement.

When Outlook began investing in Freeport a couple of years ago, the company’s need to deal with this kind of headache fell with a clunk on the “con” side of the ledger. But the “pro” side of the ledger, in addition to listing Mr. Adkerson and his team of veterans, carried this:



That accelerating curve is global copper demand, fueled by global urbanization and industrialization and by the obviously permanent craze for electric cars and trucks. They need 4 times the copper needed by gas-engine vehicles. Mr. Adkerson, backed up by nearly every copper expert, has been saying one thing over and over: “There are no spectacular new copper mines on the horizon; and even if there were, it takes a decade to develop them.” In other words, growing worldwide copper supply is tough, and worldwide demand is going to accelerate . . . which means Freeport has a very fair chance to do extremely well, over the next 5 to 10 years. We’re taking the ride with the company.

© Dave Raub  
Outlook Capital Management, LLC  
[125 S. Wilke Road, Suite 200E](#)  
[Arlington Heights, IL 60005](#)

[847-797-0600](tel:847-797-0600)

*The remarks above aren't a general recommendation to buy or sell particular securities. Such decisions should only be made in the context of an investor's own circumstances. Stocks and bonds carry the risk of loss.*