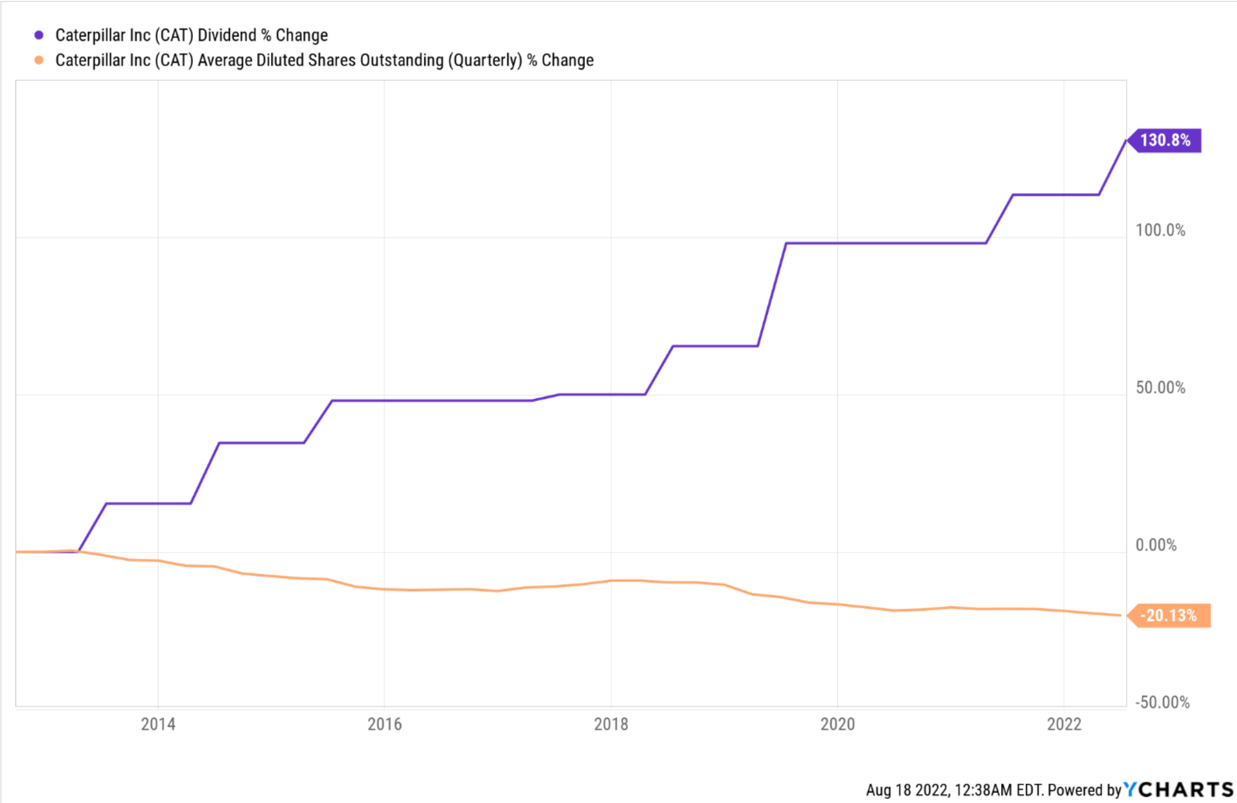
Inside Caterpillar: Last Quarter's Progress

Aug. 18, 2022

This past quarter showed Caterpillar's resilience as a company. In its Earnings Call, there was no sugar coating about the business problems it is working through: inflation causing higher freight and manufacturing costs, never ending supply chain constraints limiting production, and a strong US dollar creating foreign sales headwinds. CEO Jim Umpleby joked about having to learn a new term, "decommit", from all the times that suppliers or their suppliers have had to decommit a shipment at the last minute because of supply chain struggles. Because of this, Caterpillar isn't able to run its factories as efficiently as it did in 2019, after years of fine tuning its manufacturing processes.

Here's where Caterpillar's strength shines through. Despite all these roadblocks, it delivered 11% revenue growth. Although there are some areas of business that are weakening, like Chinese construction and North American residential construction, the majority of Caterpillar's customers are still placing orders, enough so that Caterpillar can't meet the demand. Backlog grew by $2 billion in the quarter.

Not only is strong demand expected in the next couple of quarters, but the next few years have some growth drivers as well. Caterpillar expects to see activity start towards the end of 2022 and into 2023 relating to the US's new infrastructure spending bill, and a similar bill is being proposed in Europe. While always volatile, commodity prices remain relatively high and demand for commodities is going to skyrocket with the clean energy movement, so mining growth is another positive for Cat. For the past few years, one of Cat's focuses has been on expanding its services revenue. While the company only releases services figures once a year, management alluded several times to how happy it is with its services growth, and that its investments over the past few years are paying off today.



Cat also showed its strength as a shareholder friendly stock. It raised its dividend by 8% in June, bought back $1.1 billion of stock (which equaled 100% of its free cash flow for the quarter), and announced a new authorization to buy back $15 billion of stock. <u>In the past 10 years, it has increased its dividend by 130% and bought back 20% of the company</u>. Caterpillar keeps on doing what Caterpillar does best: work through difficult market conditions, continue to both invest in the company and return money to shareholders, and set itself up for continued growth in future years.