**The Outlook: April 8, 2017**

***"Godawful" times. Wonderful people. Great investments.***

Rough times bring out the best in most people. Very rough times—yup, "godawful" times—bring out "the best" from some people which is so good it's astonishing . . . sometimes in the neighborhood of "miraculous." By the time most of us have been around the block quite often, we know this about people, and list it under the "good" column when we add up the pluses and minuses of the human race. In the investment world, however, not too many experts seem to see that when rough times bring out people's best, it quite often means astonishing investment opportunities are sitting under our noses, waiting to be picked up.

Here is a picture of ConocoPhillips' "rough times," these past few years.


The red line is Cash from Operations, a company's lifeblood. If fell from its 2014 peak of $6.3 billion to its year-ago low of $0.4 billion—as oil prices plunged from $107 to $27. That's more than "rough;" we can call it "godawful." And there in blue is Conoco's stock price, doing a screaming freefall from $86 to $33, in 18 months. Finally, the yellow cliff-dive is Conoco's dividend, cut in one step from 75 cents to 25 cents.

Conoco CEO Ryan Lance—a 30-year veteran of the oil business with the past 15 at Conoco—will surely look back on this grim time, in retirement, and say, "That was the hardest test of my business life." Conoco, the biggest "pure exploration and production company" in the global energy business (meaning it had no refinery operation to cushion the sheer pain inflicted by falling oil prices) was not quite fighting for its life, but was certainly fighting to survive as a strong, independent operator in the global energy business.

As usual, Outlook became interested in Conoco as it accelerated downhill, buying steadily in the $45 range later in 2015. We didn't buy much at that absolute $33 bottom. Nobody does, except by luck. But it

looked highly likely that Conoco had enough financial strength to give Mr. Lance time to fix those godawful problems; and Mr. Lance looked like the kind of boss who would do just that.

He has indeed. 10 days ago Conoco announced the sale of its Canadian oil-sands properties for 13 billion dollars. It was very far from the first step Mr. Lance took, to heal his company. He had already taken quite a few steps—cutting costs, trimming debt, reducing Conoco's "break-even cost of oil production" to $50 per barrel from its 2014 level of $65 per barrel, or so. But the Canadian sale was the unexpected exclamation mark, so to speak, toward the end of his turnaround story. In one fell swoop, Mr. Lance and his team have gained some mighty big benefits:

- Conoco's cost of production falls to $35 per barrel. (Oil, remember, is trading around $50 per barrel these days.) This happened because the Canadian oil is Conoco's highest-cost oil.
- Debt will fall from 2014's $27 billion to $20 billion this year, and to $15 billion by 2019, Mr. Lance promises.
- Conoco will buy $6 billion of its shares back in the market, about 10% of the whole company—giving each of us shareholders 10% more of the company without spending a dime, ourselves.
- The dividend will pick itself up off that 25-cents floor and begin rising again. Outlook suspects the upcoming hikes will not be trivial.
- Conoco's oil reserves (the truly long-term lifeblood of the company) will stay at 30 years of future production. Mr. Lance thinks $5 billion of capital spending per year (comfortable for Conoco, with its debt and cost cuts) will be enough to keep up current production and find the new reserves of oil needed to stay at 30 years of future production.

Last year, Mr. Lance told us it might take 3 years to accomplish all of that. He has done it in 1 year.

What do we do next? We wait for the global oil market to continue curing itself, as it began to do one year ago. Global oil supply <u>will</u> suffer from the tremendous cuts in exploration and production spending taken by every firm from Exxon to Conoco to Crazy Wildcatters, Inc. Global oil demand will keep growing steadily . . . more strongly because of the 2-year plunge in its cost. That's how people who demand and supply <u>anything</u> behave, when their market hands them dramatic price changes. That's why markets fix themselves, turning around and climbing higher and longer than most people can imagine when they're still shell-shocked by the plunge. Finally, that's why Outlook strongly suspects Conoco's blue, red and orange lines will be doing the same thing in the years ahead.


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