

The Outlook: April 26, 2017

The valley of the shadow . . . and Caterpillar.

Caterpillar, 1 month



Caterpillar, 6 Months



Words matter a lot. They tell us how we are thinking about things. We investors might say (to ourselves or others) “We’re investing in Caterpillar.” Or we might say (heaven help us) “We’re trading in Caterpillar,” which always sounds more dignified than “We’re speculating in Caterpillar,” which is of

course what “trading” actually means. But at Outlook we believe, with some passion, that we’d all think more clearly if, instead, we thought, “We’re handing a chunk of our life savings to the people running Caterpillar.” When we think it that way, it sharpens our minds wonderfully, so that our next thought, quite rightly, is: “And do those people know what they’re doing?”

CAT CEO Jim Umpleby and his team do indeed know what they’re doing. Caterpillar announced quarterly earnings, yesterday. The top chart shows the result: a 15% explosion in the stock over the past few days. The bottom chart adds a little more perspective: this was the second explosion in CAT in the past 6 months. The first one gave us 16% or so, also in only 2 or 3 days, with most of the rocket ride happening in exactly one day, just like yesterday. So we’re up 30% in 180 days, but most of the pleasure came in 2 of those days, and the other 170 days or so gave us the kind of waffling up and down in a “range” which spells the death of most traders and speculators, sooner or later.

Here’s the result of what Mr. Umpleby’s team have been doing the past few years.



On the left, quarterly sales grew 3%. It was the first gain in almost 3 years. On the right, CAT’s continuing profits gained 100%. And just a little more perspective: since peaking in 2012, CAT’s annual sales fell 28 billion dollars, which is about 43%. This quarter’s happy 3% uptick clawed back exactly one billion dollars of the loss. Yes . . . our company has a pretty long road still ahead of it, doesn’t it? And yet, that tiny recovery in sales triggered a 100% gain in earnings per share.

“The difficult but necessary decisions we’ve made since the downturn have resulted in outstanding operational performance.”
(Jim Umpleby, yesterday.)

That’s not quite as inspiring as Churchill’s “Never have so many owed so much to so few;” or Shakespeare’s “We few, we happy few, we band of brothers.” But the thing the “traders” never understand is that it deserves to be nearly that inspiring. There was a tone among CAT’s team, yesterday, of men and women who’ve walked through the valley of the shadow of death, and just now are glimpsing the rising road taking them out of that awful place. (This will be the literary Outlook for the year.) CAT’s people faced a

terrible crisis, these past 4 years, as the energy and commodity markets plunged, and mining and industrial equipment spending plunged with them. CAT steadily cut costs, intelligently. CAT closed its weakest factories and strengthened its best. The company helped its global dealer network get through “the valley.” Finally, because CAT entered the valley with the great financial strength built since the last crisis (the Calamity of 2008 – 2009), it maintained its dividend, kept buying back its shares, and invested in the new or improved heavy equipment which will be bought in increasing numbers for many years ahead, quite likely, by the same customers who had to hunker down and stop spending in the depths of that valley.

A couple of days delivered 30% gains, surrounded by months of going nowhere while a tidal wave of pessimistic analysis from the trading crowd washed over CAT’s stock. (“This stock is way ahead of itself, way out on a limb, nothing can justify it, run for the hills,” etc.) “We’ve handed the folks running Caterpillar a chunk of our life savings,” is the only way of thinking liable to carry us investors through those 180 days, so that we were strapped in for the ride before it happened. Nobody expected it to happen yesterday, from Wall Street’s finest analysts to the day-trader next door. When good people face a crisis and go all-out to fix it, remarkable things aren’t surprising, they’re certain. They’re also “eventual,” of course, which is another important word for good investors to use, whenever we think about our business. At Outlook we think that “eventually” Caterpillar is going to claw back all of the \$28 billion in sales lost since 2012. We won’t put a number to what that will mean for CAT’s earnings and share price . . . but this quarter is a pretty good hint.

© 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.