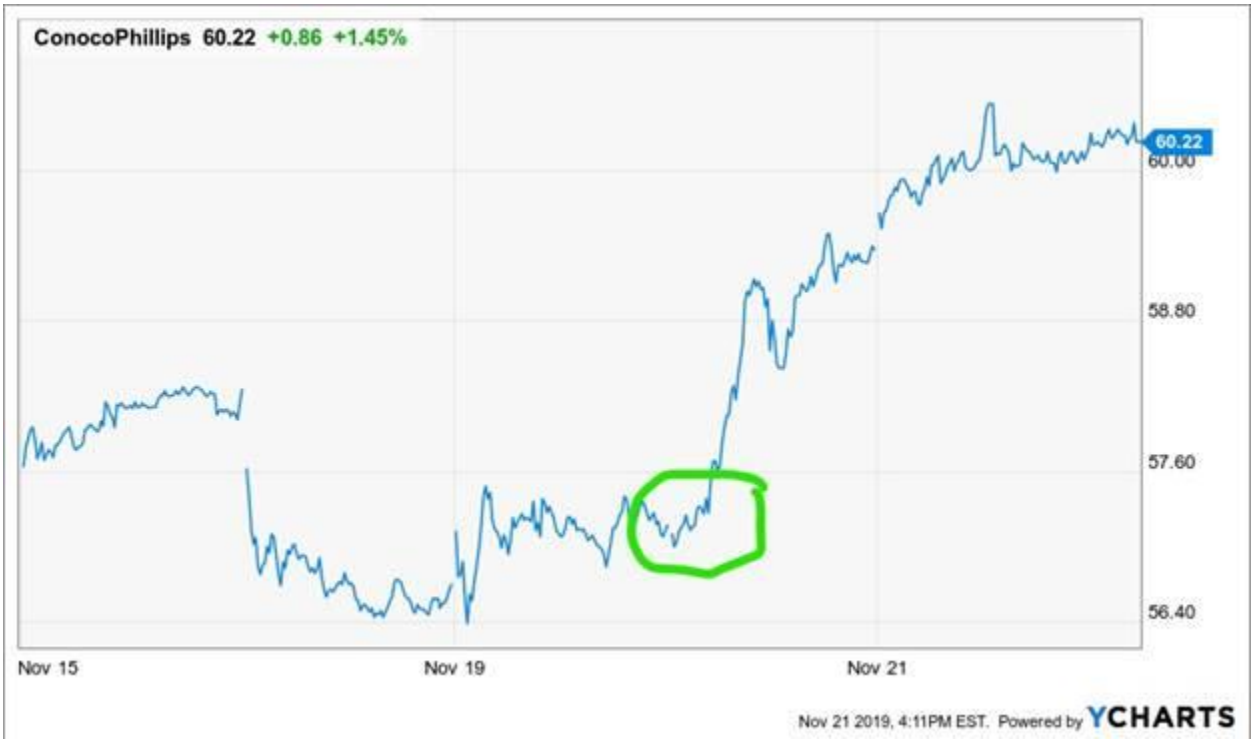
The Outlook: Nov. 21, 2019

"We will show you."
(Conoco, to the investment world.)

Conoco did something genuinely remarkable this week. It deserves that underline, because only 6 weeks ago Conoco hiked its dividend 38%. *That* was remarkable . . . but it only set the stage for this week, when the company published a "10 Year Plan," which spells out exactly how Conoco aims to run its oil-exploration business from 2020 – 2030, *and* how it aims to reward its investors. It's one of the most impressive, and most unusual documents Outlook has seen in 42 years. It is a giant company, operating in a fearfully volatile industry, committing itself to delivering outstanding business performance and shareholder rewards for the next decade—and convincing us that they'll damned well do it. (Texas oilman talk—oil women, too.)

The market often swallows hype and nonsense whole, when they come from its "celebrity" companies; but sneers at the near-miracles performed by Main Street's hard work and good management until they're too clear to ignore. But it had a little trouble sneering at Conoco, as this picture shows.



It had that trouble because over the last 3 years Conoco has backed up words with actions—actions which, instead of falling short of the company's promises, have nearly always gone well beyond them. So when CEO Ryan Lance and team took about 2 hours and 121 slides to tell Wall Street's most prestigious analysts what Conoco will do by the year 2030, and how much cash it will deliver to shareholders, the analysts were inclined to take Mr. Lance seriously indeed—no matter how astonishing his commitments might seem.

Here are the highlights:

Conoco: $50 Billion to Shareholders Over 10 Years . . . at Oil Prices Lower than Today's

Oil today (West Texas Intermediate) is at $57/barrel. Conoco's plan is based on a starting price of only $50/barrel, rising 2% with annual inflation, so ending at $61/barrel in 2030. The price of oil is the only part of the 10 Year Plan which Conoco can't control, or at least effectively manage. Mr. Lance's assumption about the future price of oil is not a "worst case scenario;" but it's not even close to a "best case scenario." It amounts to saying, "The price of oil is going to go up and down, no matter what. Let's plan around a price somewhat lower than today's—which no knowledgeable people regard as "high," regardless of their differing opinions about the future."

That's called a "conservative" assumption. If it comes true, Conoco has committed to generating $50 billion of free cash flow by 2030, and returning all of it to shareholders: $20 billion in dividends and $30 billion in share buybacks.

- That $20 billion in dividends would allow Conoco, beginning with today's 38%-hiked dividend, to grow the dividend 7% to 8% per year: today's $1.68 annual dividend will reach $3.46, and yield 5.8% on today's $60 stock price.

- That $30 billion in share buybacks would almost cut Conoco's share count *in half*. Each share we own today would have double today's claim on Conoco's earnings, as of 2030. We used the words "remarkable" and "outstanding" a few times, above. If we had to apply those words to just one promise from Conoco, this is it.

There are more "remarkable" points in Mr. Lance's "10 Year Plan on a Page," up there. His company will generate positive free cash flow at an oil price of only $35/barrel—not much higher than the $27 "Death Valley" number to which oil plunged in 2016. Conoco's leverage ratio (reflecting the risk of its level of debt) is less than 1 throughout the decade. That's an outstanding number, meaning "no appreciable risk,"

and it's there because of the outstanding work Mr. Lance and his team have done, down there in Death Valley, since oil dove off its cliff in 2014.

The next chart just touches on some of that work.

Conoco: Hurting in 2015 . . . Invulnerable in 2019

And our last chart is Mr. Lance saying, in essence: "Here's how our shareholders got hurt; and here's how we're making it up to them, and making sure they never get hurt again."

The rebuilt Conoco will make money "across the cycle:" when oil heads toward Death Valley, and when it heads toward Everest. The Conoco team did this by cutting down debt with an ax: from $24 billion of "net debt" (debt minus cash) to $6 billion, in 3 years. It managed that job by selling oil fields which were good . . . but not Conoco's best. By shrinking the whole company like this (while keeping its best fields), it drastically lowered its "cost of supply" of each barrel of oil from as much as $60 to today's $40, heading lower toward $35. By building up cash-on-hand and keeping it on hand, it gave itself the strength to ride out oil's roller coaster cycle and keep investing in its business—and keep paying free cash flow to shareholders.

More than one of the Wall Street types listening to Conoco, yesterday, told Mr. Lance, "We've never seen anything quite like this Plan." At Outlook we feel the same way . . . not counting the "castles in the air" kinds of plans routinely issued by the likes of Tesla, Uber, WeWork and friends. This is not a castle in the air. It's a dead-serious commitment to Conoco's shareholders, coming from people who've shown they mean what they say. At Outlook we suspect Mr. Lance and his team have set an example which will be followed by much of corporate America, in the years ahead.

Just one more picture.

Caterpillar: Sticking with a Good Plan and Good People for 20 Years

Investing is not a game, a computer program or a betting scheme. It's not luck. Above all, it's not something "too complex" for ordinary people—though the investment world works overtime, peddling that notion. Investing is recognizing what truly determined people do with their companies all the time. They overcome terrible problems; they build astonishing financial strength; and they deliver astonishing returns as a result. But many investors can't shake an inner feeling that maybe the game, the program and the betting schemes are what really matter. Those investors always fail, because when those "red arrow" plunges into Death Valley come along—as they did for Caterpillar, above—their fears swamp their faith in the power of Main Street's determined people. But we can see, up there, how well such faith pays off. Beginning near the top of the "Dotcom Bubble" 20 years ago, Caterpillar has returned almost 5 times the market's returns. That's how "value investing" works at its best. At Outlook we strongly suspect that Conoco has just raised its hand to the market, and said, "You may decide what you choose to have faith in, for the next 10 years. We're going to show you."

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