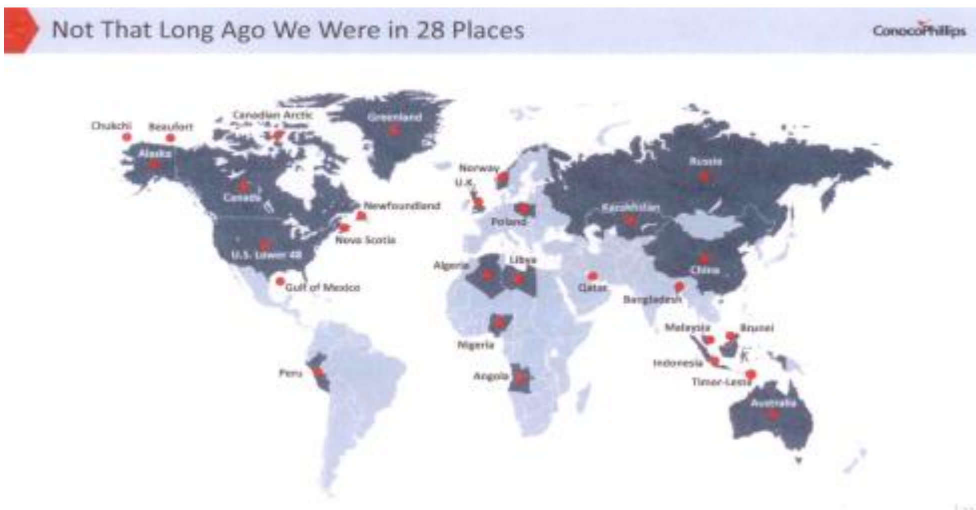
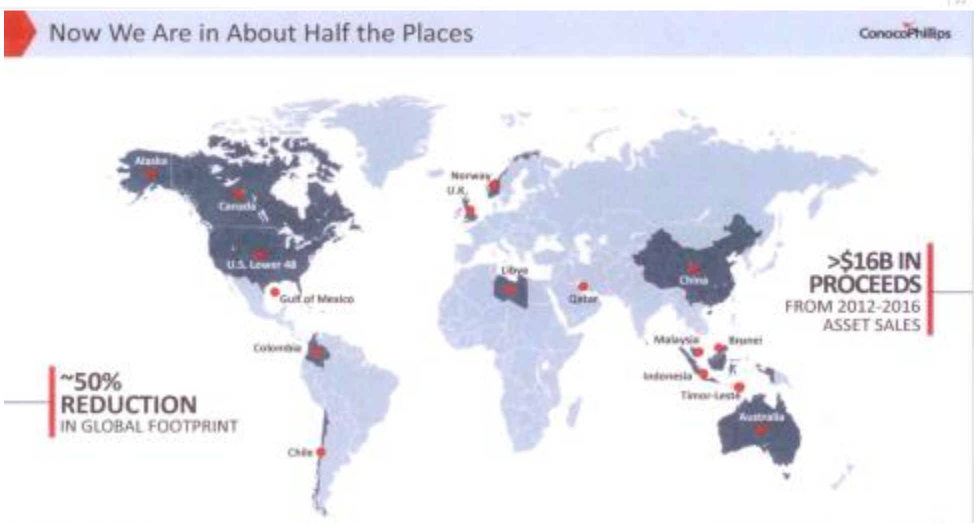
The Outlook: Nov. 18, 2016

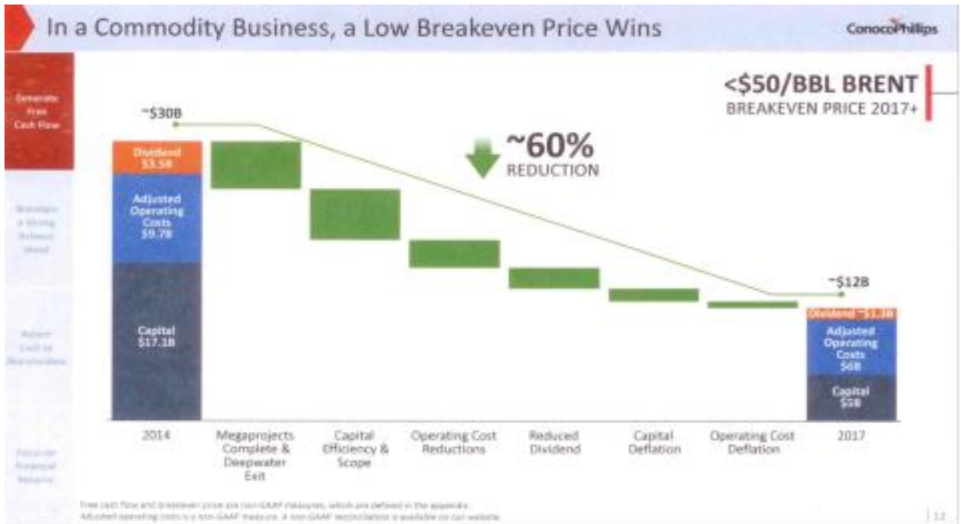
Conoco and Geospace: intense pressure, admirable leaders.

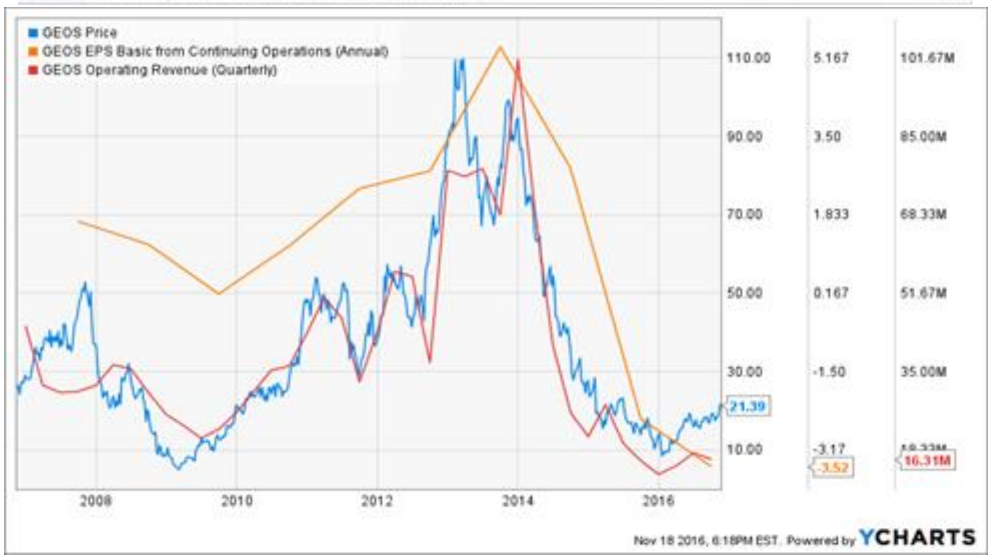
History, at its very best, is such a treat because it shows us how real people behaved under intense pressure. We can't help but stand in awe of how well many historical figures behaved through whatever their trials happened to be. And when the historian herself is a person of sympathy and understanding, we find ourselves sharing those feelings toward the many, in history, who stumbled or fell during their trials. (Unfortunately a great many historians' fundamental attitude is condescension, which naturally distorts everything they wish to tell us about.)

Watching how business leaders behave under intense pressure isn't just a treat, it's a money-making practice. The oil industry has been the best place of all, these past 2 years, to see some very good CEO's rising to the toughest trials of their careers. Two of them run Outlook core companies: giant Conoco's Ryan Lance; and tiny Geospace Technologies' Rick Wheeler. Let's glance at some charts.









That's a lot of charts! Here's the fast takeaway.

The top two show the chainsaw Conoco's Mr. Lance has used to bring down his company's costs, in the survival crisis caused by oil falling from $110 to $27 since 2014 (before rising to today's $45.) Conoco, the biggest U.S. "pure" oil producer, has completely reversed its long-term business strategy. That drop from 28 global locations to 14 (or so) was the engine behind the 3rd chart, which shows Conoco's annual capital spending plunging from $17 billion to $5 billion in 2 years. <u>A 70% cut in drilling and production spending is a stunning change.</u> Most veterans of the business world live through cost-cutting crises at some point (or points) in their careers. They're not in the least fun; the pressure to do them fast, but right, is intense; and the 2 years Mr. Lance has spent at this particular task will have felt to him like 10 years, at times. But he has succeeded, and what he did might not deserve the word "miracle," but it's been a gold-medal achievement. Because of Conoco's remarkable spending cuts and asset sales, its corporate debt is also plunging toward a level, by 2018 – 2019, which will allow Conoco to prosper, and handsomely reward us shareholders, in good and bad times for oil, and everything in between.

The 4th chart is Mr. Wheeler's story, at tiny Geospace Technologies. Geospace had its quarterly Earnings Call a couple of days ago, and its story was the horrifying business equivalent of Frankenstein and Dracula combined. Every one of its flagship product lines (seismic equipment for discovering and monitoring oil fields) fell in a way which can only be called "terrifying" . . . and as Mr. Wheeler drily remarked, "This is our third straight year of falling sales—the worst period in our history." The red line, above, is those plummeting sales; the yellow line Geospace profits; and the blue line its roller-coaster stock price. ("Cliff-diving" covers it a little better, doesn't it?)

Now, let us focus on the strangest thing about this terrible picture. Not only has there been no good news this year—there's been nothing but increasingly god-awful news (pardon the French.) But while Geospace plunged to around $8 per share in January . . . now it's at $21. For heaven's sake, why?

As Outlook has noted quite often, the market is a strange combination of foolish and wise. It takes turns between the two, and often does 'em both simultaneously. Mr. Wheeler and his team in Houston have been around the block very many times, in the oil business. They built their small company around cutting edge seismic technology . . . and zero debt. Geospace has $67 million in liquidity right now (a lot, for its size and needs), and Mr. Wheeler knows it will survive the downturn in spending from customers like Conoco and every one of its peers. He's been around the block, and he built the company to survive a crisis. And when seismic spending comes back (which it absolutely must do, because the brake-slamming since 2014 will have a mighty effect on global oil supply within a year or two (or three), Geospace will see profits rise like that proverbial rocket, on anything close to the level of sales it had 3 years ago. The company made $5.40 per share in 2013. Today's $21 share price simply shows that the market is wise enough to understand that this future is going to happen, for Geospace . . . but it is cautious and anxious enough to only value the company at $21, rather than the $40 to $60 neighborhood in which it will stand, when those earnings eventually return. We're not immune to caution and anxiety . . . but we aim to offset it with the kind of patience which makes real money for investors.

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