

The Outlook: September 19, 2020

In the arena: Freeport builds a happy ending to its long story.

There's a very old-fashioned story behind this picture—a story which has taken more than 10 years to unfold. It's a story of bad luck and big problems at a company . . . and about the extraordinary determination and ability of the company's grizzled veterans, who tackled the problems over those 10 years. Just lately it's beginning to look, to the market's mob of speculators, as if this story will have a happy ending—hence the green arrow at the right, showing Freeport McMoRan's 220% rocket rise since the Virus Bear Market bottom in mid-March. The near-certainty of that happy ending, of course, has been perfectly obvious for several years . . . to investors with enough interest to dig into the story, and enough patience to wait awhile for the ending. Here's the summary:



- Red Arrow, Plunging Down: 2011 – 2016.

That was the copper market crashing down by 60% or so, from 2011 to 2016; and the oil market plunging 75% or so, even faster from 2014 to 2016. Copper and oil are commodities, and they will live in their cycles, always. Freeport, which is pretty much the world's Copper King, had lived in its copper cycle for decades before 2014, but had the bad luck to buy into the oil business near the top of oil's cycle . . . and borrow the money needed to do it.

- Green Circle, 2016 – 2020.

That's been those grizzled veterans facing and fixing the problems—some of which looked pretty frightening. Among other things, Mr. Adkerson and his team somehow sold the oil properties at

rather good prices (because they were rather good properties); cut Freeport's debt by 80% or so; calmly and diplomatically defused a wholly illegal attack on their rights and contracts by the government of Indonesia, which threatened Freeport's crown jewel copper-and-gold mine; and pulled off a difficult and risky technical-mining project, converting Indonesia's Grasberg mine from open pit into underground. (Grasberg sits on top of a 15,000-foot mountain in Papua—a location which makes Indiana Jones' travels look like tourism at 5-star hotels.)

- Green Arrow, Rocketing up: March 2020 through today.

As Outlook has noted a few times, the market's speculating crowd reacts by the hour and minute to every piece of news (true or false) and every vague impression about the news which passes by, courtesy of both the media and the nonstop rumor mill which works in all crowds of human beings who are intensely focused on the same thing (their money, when the crowds are the investment world's speculators.) On the bad side of that truth is the roller coaster it creates in the market—because hair-trigger speculators are such a vast crowd, compared to patient investors, that they absolutely dominate each day's market behavior. On the good side is the fact that while bad news and silly impressions do their damage, good news and (especially) the cash earned and paid out by Main Street's operating businesses can never be ignored. Cash speaks louder than distorted impressions or nightmares—and always makes the market's speculating mob see reality, eventually.

Let's listen to Freeport's Chief Financial Officer, Kathleen Quirk, talking about her company, last week:

At Grasberg we expect to be 70% done with our block cave (underground mining) spending in the fourth quarter. By middle of next year, we expect to be 90% of the way there. *This completely changes the cash flows of the company.* We're already gotten to creating free cash flow in the second-half of this year, and that'll accelerate as we go into 2021 and beyond. So we have very positive momentum in getting the expansion done. And as you all know, we're relying on our 50 years of experience in Indonesia and our high-quality technical capabilities in Block Caving.

At our Cerro Verde mine in Peru, which was impacted earlier in the year from a government-mandated shutdown, that's recovered nicely. We're continuing to ramp-up production there, and we're hitting the numbers according to our plan. The team there has just done exceptional work in managing through this difficult situation, ramping back up and doing it safely. So that's running according to plan. And we're pleased to also say that our U.S. Lone Star project is being completed. This is a brand-new mine in Arizona in our backyard, where we've operated for decades, and that's gone really well, came in under budget, on time. And so that's going to start adding to our free cash flow.

We're in a very good position. We're foremost in copper. And copper is more and more a strategic metal, particularly as the world moves towards decarbonization. So we're very well placed. We've seen global copper inventories decline this year, which is striking, because during the middle of a pandemic, you would expect to see inventories of products like copper rise dramatically instead of falling.

It all really sets us up for the long-term as we look forward in 2021 and beyond, as the whole global economy begins to improve, gives copper a real shot at another leg up and Freeport is really well-positioned there, with very long life reserves and possibly the best group of copper mines in the world. Putting this together, we're very focused on cash flows. As I said, we'll be generating free cash flow beginning in the second-half of this year. We've managed through the trough. And as we increase production at Grasberg, it really changes the complexion of our company. You'll start to see very significant cash flow generation, putting us in a position to begin to continue to strengthen our balance sheet and consider resumption of cash returns to shareholders.

So we're not changing our plan. We're being very deliberate about execution. We're very focused on execution. And we think that if we continue along this path, executing strongly against this plan, we believe that this plan will deliver exceptional value for shareholders. There's still risk in it. We understand that. We need to execute. We need to continue to overcome challenges. But our team has been working on this project for a long time. We've been investing in it for 15 years. We want to see it through. ***We want to see our shareholders get the value from this plan as opposed to other shareholders getting the value.***

Ms. Quirk's last remark, in bold up there, was a reference to the fact that Freeport is suddenly looking like a wonderful merger candidate . . . to companies which have fallen far short of Freeport's achievements through its 10-year story.

None of that story has been mysterious or hard to understand. It's a story which happens on Main Street all the time: tough problems, bad luck, hard work fixing things, happy endings. But (as Outlook has also noted a few times) the kinds of people who work on Main Street are fundamentally different than the kinds of people who work on Wall Street (its speculating mob, anyway.) Main Street works every day with bad luck and rough problems, and endlessly carries out the hard work needed to fix them. Main Streeters are "in the arena" all the time, with complete individual responsibility for results. Wall Streeters, though, are much more like Mr. Roosevelt's "critics sitting outside the arena," who never stop talking and betting, but do not act. Freeport-McMoRan is Main Street at its best, and in the years ahead we'll be surprised at just how happy an ending its people have built for us.

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