<u>The Outlook: April 2, 2020</u>

"Oil Surges 25%!" tells us nothing about tomorrow . . . but a great deal about a principle.

What the oil market did today was enjoyable, for us energy investors, and it's OK to spend a moment admiring today's chart. But there is a much deeper and broader lesson here for all investors, oil or not. First let's smile at the chart.

Thursday: Oil (orange) and Conoco (blue)

Only a couple of days ago we remarked that "Blood in the street, in oil, means what it always does." (Buy.) We hadn't the faintest idea that two days later we'd see this headline:

"Oil Surges 25%! Biggest Percent Gain Ever on Supply-Cut Hopes!"

And we haven't the faintest idea what will happen tomorrow, or the next day, week or month. The market's giant speculating crowd doesn't know either, but they'll bet on it anyway—because that's how they try to make a living. None of that really matters. <u>What does matter, enormously, is that we investors truly understand the nature of the markets—and we keep that understanding in front of our minds no matter how terrified or exultant the market's current behavior and the media headlines happen to be.</u> If we do, we'll always succeed. If we don't, <u>we will fail</u>. Sometimes the truth is stark and simple, and this is one of those times.

The nature of the markets is that speculators drive prices, all the time. They bet on the impressions created by the daily news. When that news and its impressions are unusually awful or wonderful, the speculating crowd bets all together, in the same direction—so the market moves up or down by startling amounts—fantastic amounts, sometimes. But no matter how "together" the crowd is, every member of the crowd always has his eye peeled on "tomorrow's headlines" so to speak: that is, the crowd is instantly ready to close out one directional bet and make the opposite bet, if the next morning's news leans toward "wonderful" rather than "awful."

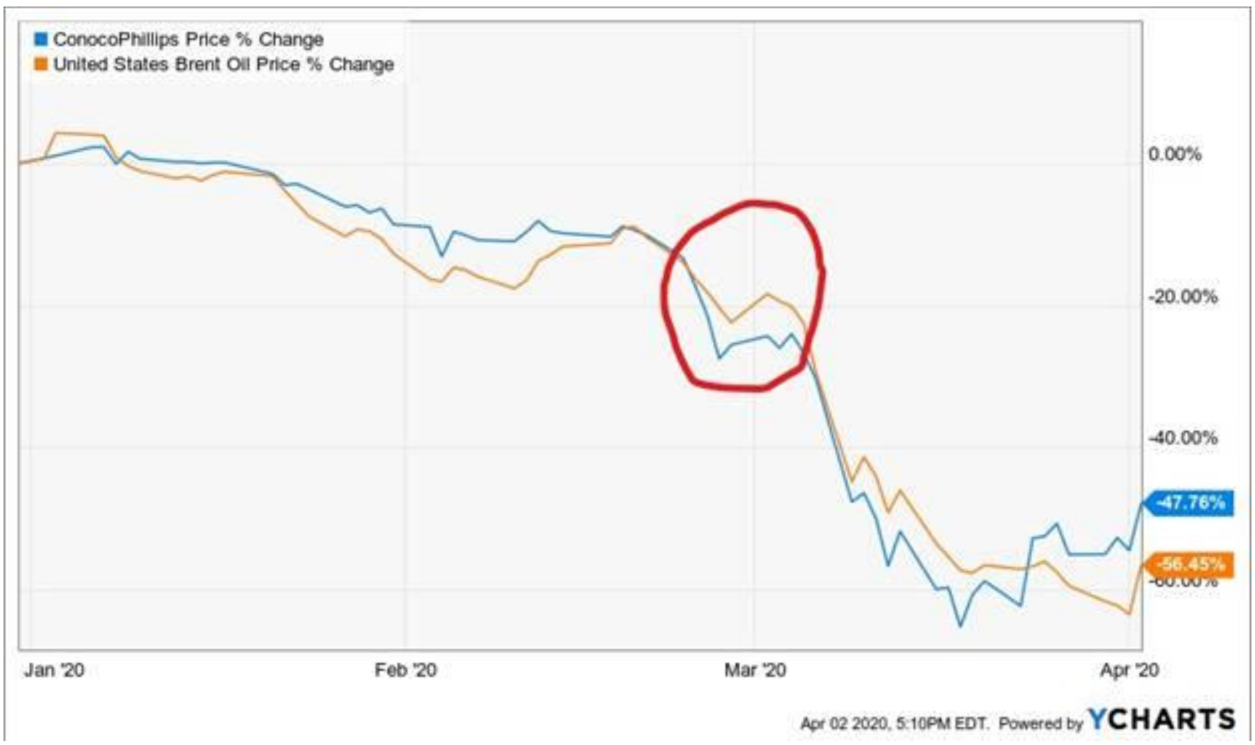
The market is merely the engine which delivers capital to the strongest, most inventive companies in the world; so it gets a big share of the credit for the historically unbelievable wealth and well-being created by the world's free market, capitalist systems. "What kind of crazy way is that to run the ship?" we might ask. "Why do gamblers have to be in charge of such an important thing?"

The best answer is "Because it's a <u>free</u> market, above all else . . . and because <u>the gamblers must also pay attention to the good news, when it shows up, if they want to make money or even survive</u>. In a free-market, capitalist economy peopled by inventive and determined individuals and companies—who are accountable for results—there will <u>always</u> be a great deal more good news than bad, over time.

That's the heart of all this: the market, the economy, the historical miracle of growth and wealth in America and every other country which has based its future on the foundation of that kind of freedom. It helps a great deal to keep that in mind when we're suffering through the kind of "end of the world" atmosphere which comes along with some regularity. (But not too much regularity, thank goodness.)

Here's another picture:

Oil and Conoco: 2020 So Far



The red circle is roughly when the Virus Shutdown and the Saudi/Russia Price War teamed up, as if they'd rehearsed it, to clobber the oil market and oil stocks. Both oil and Conoco happened to begin the year around $65 . . . and we can see the screaming cliff-dive which came next: oil from $65 to $20 or so; Conoco from $65 to $22.

The market's giant speculating crowd hadn't the slightest difference of opinion. It acted with one mind, betting "Down!" with every borrowed dollar it could scrape up. And when oil got to $20, just the other day, did that price mean anything to the crowd? Had the crowd reasoned its way to the studied conclusion that $20 was a fitting "valuation" for oil, and $22 was the same for Conoco, given all that was known or knowable about the oil market and Conoco, two days ago?

As the old saying goes, "Cue the sound of crickets chirping." No, regardless of that hallowed academic contribution to the investment world called the "Efficient Market Theory" (which for 50 years has informed us that today's stock prices, no matter what, do indeed reflect everything "known or knowable" about, well, everything), <u>the only meaning</u> behind $20 oil and $22 Conoco was that they were "Down! A lot!" from where they were before the awful news created its terrifying headlines in March. And the only meaning behind today's "Oil Surges 25%! Biggest Gains Ever!" headline was that a piece of news came along which actually hardly means anything . . . but which told the speculators it was high time to think about reversing that unanimous bet on "Down!"

The news item—that Russia and the Saudi's might make a whopping production cut, together, to support the price of oil—is almost as silly as the earlier news items which reported, with wide eyes, that they were both going to "open their oil floodgates" by 10, 20 o 30 percent. That was nonsense, because neither is able to come close to that . . . but it made good headlines. And today's headline that the two combatants might "cut" 10 million barrels per day of production is the same sort of nonsense. As we noted a couple of days ago, in a fairly short time the world's storage capacity will be used up, forcing producers from Texas to Siberia and the Persian Gulf to shut down wells. None of them want to do that, because all know it's a drastic action with long-term damage to future production . . . but it's going to happen anyway, because for the next few months, at least, the world's need for oil will drop like a rock due to the Virus Shutdowns.

But the simplest way to say it all is: "After a great big "Down!" bet, which was overdone as it always is, it was time for the first "Up!" bets.

It is a funny way to run a ship. But it's not random or unpredictable at all. It's as predictable as "The cure for low prices is low prices" principle says it is. The challenge for real investors, as always, is having the patience and endurance needed to stick with the principle.

© Dave Raub
Outlook Capital Management, LLC
125 S. Wilke Road, Suite 200E
Arlington Heights, IL 60005
847-797-0600