



A Rodney Dangerfield Market August 10, 2010



William Smead
Chief Executive Officer
Chief Investment Officer

Dear Fellow Investors:

I love to watch the biographies on CNBC and on the A&E Channel. Rodney Dangerfield's biography was on last week. Born Jacob Cohen, Rodney worked as a comedian for years as Jack Roy. He floundered a long time, but he worked hard perfecting his jokes. He ultimately broke through nationally by appearing on the "Tonight Show" and on "The Ed Sullivan Show". His agent gave him the name, Rodney Dangerfield, after a character in one of Jack Benny's old shows. His career exploded when he came up with his trademark introduction, "I get no respect". Most of his jokes were attached to less than great things which went on in his life whether real or fiction.

At Smead Capital Management (SCM), we go through phases when we feel a little like Rodney. We are a large cap value firm with a series of eight criteria. These criteria seek to guide us to companies which have demonstrated: 1) success in the past, 2) have strong balance sheets, 3) have wide moats to protect the duration of their profitability, 4) generate high levels of free cash flow and, 5) are available at below market PE multiples or are available for purchase at 30 to 50% below intrinsic value.

When we go for an extended period of time with markets not recognizing the merits of our portfolio we can feel a little sick. Rodney went to the doctor because he felt a little sick. The doctor told him, "Rodney you are sick." He says, "Can I get a second opinion?" The doctor replies, "Yes, you are ugly too." We believe to make above-average returns in an expense minimizing and tax efficient way, you need long duration investments. Low turnover promotes low trading costs and lays the groundwork for the kind of wealth creation that only comes from having a significant part of a portfolio invested in stocks which garner long-term dividend growth and trade at many times original investment ten to twenty years later. Can we at SCM pursue anything more contrary to the conventional wisdom and popular investment approaches of today? Holding periods on the New York Stock Exchange are the shortest ever recorded in recent years and portfolio turnover among large cap equity mutual fund managers is close to all-time highs.

Even if you have a reason to believe that you own superior companies and are patient enough to hold many of them for years to receive the long term benefits, you can temporarily feel ugly too. One day you come in and the market is down because of the fear of our economy collapsing. The next day investors are chasing the hot commodity or ETF of the day. Rodney would say, "It's tough out there." Based on trailing and consensus estimates of non-GAAP earnings, our companies trade at sizable PE discounts to the S&P 500 Index. This is despite having superior ten-year records of revenue and earnings growth in comparison to the S&P 500 Index. Rodney said, "I get no respect. I play

hide-and-seek, and they wouldn't even look for me." Individual and institutional investors rarely seek out a portfolio when its style is out of favor and the most future success is available near the lowest prices.

We believe difficult markets are a great time to hone your craft and patiently wait for the benefits of buying and holding well-chosen common stocks. They were many times when Rodney felt like giving up, but ultimately he attained wealth and fame at the highest levels of the entertainment industry. His on-stage persona and trademark lines differentiated him from other comedians and caused him to bond with a large group of fans covering three generations. We believe that many of our portfolio holdings could have very bright long-term futures, even though at the moment, they are a little short on respect.

Best Wishes,

William Smead

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