## Freshmen in College

**William Smead**
Chief Executive Officer
Chief Investment Officer

Dear Clients and Prospective Clients:

Everyone who goes to college wants to earn a bachelors degree. Many young people show up at college as freshmen and get off to a very difficult start. I was one of those freshmen. My first set of mid-semester tests showed that I had learned the subject matter in an underwhelming way. I was unable to separate the significant from the insignificant. I also tried to get by with an unusually good memory and a below average amount of time spent on studies. Fortunately, my professors had seen many a cocky 18-year old roll through the halls of Whitman College and took mercy on me. They said that they would grade me for the semester on improvement and that I needed to buckle down.

The first year of college you have four main problems. First, you are forced to establish a life pattern without the walls to bounce between which had been set up for you by your parents and your community. Second, the complexity of the classes and the mental disciplines to be learned were geometrically tougher than high school classes were. Third, you weren't yet trained to cull and analyze information for what is important, which caused you to dwell on the interesting but seldom important parts of the material. Fourth, the people I was competing with for grades were folks who came into the process with much better study skills and way fewer sports and social interests than yours truly.

Why do I bring this up in an investment blog? This huge decline in the stock market the last 18 months has thrown us outside the walls we used to bounce off of. Many of us want to transfer to an easier school (CDs, Money-Market funds, T-bills, etc.). We are overwhelmed by 24-hour news and the internet burying us in information about what might happen in the short run and some of the most believable opinions are very complex. We are more attuned to the information about the next couple of months than we are about the next 5 to 10 years. Lastly, fear is driving us to extrapolate the negative and envy those who have temporarily sidestepped some of the decline. It seems like they have better investment study skills.

Since I turned things around and graduated with a solid GPA from an academically tough school, please consider the opinions of Smead Capital Management on what doesn't matter in the long run and what does.

***What doesn't matter!***

1) Stocks could go down more in the short run.
2) The economic contraction could last longer than the non-pessimists think.
3) Inflation could run wild if we have a strong recovery.
4) Oil could have a big price increase in a strong recovery.

***What does matter!***

1) When U.S. stocks have produced a negative return looking back over the prior ten years, they have produced a positive 14.5% return on average the following ten years (Four prior instances--1875, 1895, 1919, 1974). The average of these four events has quadrupled stock portfolios in 10 years if dividends where reinvested. Stay in school and don't transfer. Buy if you have cash.
2) Stocks are cheap in relation to normalized profits and U.S. economic output (GDP).
3) There is 50% more cash on the sidelines at this low point relative to stock market capitalization than there was at the bottom in 1974.
4) Companies are starting to buy each other (IBM is buying Sun Microsystems, Pfizer buying Wyeth and Merck buying Schering Plough).
5) Oil was a bubble as recently as last year and bubble markets which break take years to put back together. Just ask investors in the Tech-heavy NASDAQ, which peaked at 5000 early in the year 2000, who learned the hard way with no significant success in nine years. I'm glad that commodities are not collapsing in price, but it will be years before they are the place to be again in our opinion.

Hang in there because we will all be sophomores soon.

Warmest Regards,

William Smead

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