Good News at the Bottom

William Smead
Chief Executive Officer
Chief Investment Officer

Dear Clients and Prospective Clients:

I read an interesting book recently by Russell Napier called <u>The Anatomy of a Bear Market</u>. He sought to dispel myths about what happens at low points in the stock market. He examined the market based on the point in time when you would have done the best over the following twenty years. He focused on July of 1932, April of 1942 and August of 1982. His thesis wasn't that buying at a major low point is all that mattered, but rather the best starting points produced forward success. For this reason he left out the market low in December of 1974.

Once he had identified the best points to enter the market over the last 108 years, he then researched what was going on in the economy. He wanted to dispel the myth that there wasn't any good news at the bottom or best buying point. He found a few good clues to look at to see if the low point had forward looking merit. First, he found that commodity prices firm up around the bottom. Second, auto sales pick up. Major companies cut their dividends close to the bottom. For example, General Electric and AT&T cut their dividend within a month of the bottom in 1932. Lastly, overall business shows some life.

Where are we now? The decline in stocks of 53% from October of 2007 to March 9th 2009 is the worst decline since the 1930's. Commodity prices have firmed as Oil and Copper prices have rebounded. Auto sales have not yet rebounded. General Electric, Alcoa, Wells Fargo and other major companies cut their dividend. Overall business conditions are showing signs of improvement. Durable goods orders were better than expected and retail sales were better in February than expected. Home sales were up on both new and existing homes. And the most active home sales are in California, Arizona, Nevada and Florida. We've had four of our clients buy a home in the Phoenix Valley in the last 60 days! Can you hear the rhyme?

We continue to believe that there has never been a better time for investors with a three to five-year outlook to buy quality common stocks. Be careful. If you wait for auto sales to improve, you could get caught in a melt up. Remember, there is more money on the sidelines than at past bottoms on both an absolute and relative basis. Did I forget to mention that the cash on the sidelines pays very little in interest?

Warm Regards,

William Smead

The information contained in this missive represents SCM's opinions, and should not be construed as personalized or individualized investment advice. Past performance is no guarantee of future results. The securities identified and described in this missive do not represent all of the securities purchased or recommended for our clients. It should not be assumed that investing in these securities was or will be profitable. A list of all recommendations made by Smead Capital Management with in the past twelve month period is available upon request.

This Missive and others are available at www.smeadblog.com.