Mini 2008
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Chief Executive Officer
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Dear Fellow Investors:

After the big move up in US stocks beginning in March of 2009 at around 676 on the S&P 500 Index and carrying to mid-April of 2010 to around 1220, you could expect a correction in stock prices. We have a theory at Smead Capital Management that the markets will do whatever they have to do to frustrate the most people. In this particular case, the most frustrating thing that the markets could do would be to put the folks who stayed in common stocks through a correction. This correction would include at least two violent downswings and would reopen everyone's memories of what happened in the US stock market in 2008. This correction is kind of a Mini 2008.

As if we needed reminding, the bear market which began in late 2007 and ended in early 2009 was the worst decline in the US since the 1930's. From peak to trough the S&P 500 Index dropped 53%. It wasn't only the decline itself that was so painful, but it was the across the board selling that regularly hit the market which added salt to the wound. The decline seemed to have no regard for the quality or the future of the companies involved. This made the bear market extra disconcerting. Disregard for shares of companies with better balance sheets and consistent earnings and dividends bothered long-time money managers like us. It was also the culmination of one of the worst decades that the US stock market has ever had. To say that confidence among money managers and common stock investors is low would be a big understatement.

After the splendid rebound from the March 2009 lows it was likely that the market would correct and reestablish a new wall of worry. We've seen a number of corrections in 30 years in the investment business. In our opinion, this one is attempting to look the most like the declines of the prior bear market as any we've seen. In the process, the wall of worry has erected itself quickly and done so with a magnitude normally associated with major market bottoms. The list of negatives is long and includes:

1. European Sovereign Debt Woes
2. The Worst US Oil Spill in History
3. No significant rebound in housing
4. Fears of a slowdown in China
5. Doggedly High Unemployment
6. Double-Dip Recession fears
7. Low Confidence among Consumers
8. Ten-Year Treasury Rates below 3%

We could go on, but we think you get the point. At this moment, we think the wise thing to do is to ask what companies do we want to own for the next five years and ignore the temporary news. Not because it doesn't matter, but because it will be replaced by some other bad news in a couple of years. Instead we want to focus on the growth in the use of PayPal and other EBay services. We focus on the rebound in business at Nordstrom or Disney. We love the consistency of business at Merck, Johnson & Johnson and McDonald's and want to be part owners. By the time that everyone quits equating every market decline with the bear market of 2007-09, we believe we will have made very solid returns in the US stock market.

Best Wishes,

William Smead

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