



## The Vision Thing

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

Dear Fellow Investors:

When the first President Bush failed to get re-elected in 1992, many considered his lack of a vision or agenda for the country to be his primary downfall. It seemed he wanted to be the custodian of the country as opposed to a leader who had a place he wanted to take the USA as a country. Voters like a vision from their political leaders, no matter whether the vision is tilted from the left or the right.

We at Smead Capital Management think about “the vision thing” as it pertains to the companies which meet our eight criteria for stock selection. Over long periods of time, it makes an enormous difference if you are invested in companies that have a clear agenda. It is a key component of our shareholder friendliness criteria. The CEO and executive team are seeking to make the vision happen by using the free cash flow of the company judiciously and in a very focused way. Any free cash flow not needed in executing the vision is then returned to shareholders through dividends and stock buybacks.

The current stock market correction is a perfect time to examine the behavior of the leaders of our companies. We will focus on three of our current holdings, Starbucks (SBUX), Nordstrom (JWN) and Abbott Labs (ABT). Starbucks had a small group of portfolio managers, which included us, into their headquarters recently for a morning meeting with CEO Howard Schultz and CFO Troy Alstead. Their vision for the company and its growth looks to be on three fronts. First, they will grow the store count around the world thoughtfully, and simultaneously seek to grow revenues in older markets like the United States. Howard pointed out that the company only has 700 stores in China. This compares to three in our company’s building in Seattle and 150 locations on the Island of Manhattan. A dramatic slowdown in the Chinese economy would not affect their vision.

Second, Starbucks is making a big push into the middle of the gourmet coffee market through its Seattle’s Best Coffee brand. Burger King, Subway, convenience stores and vending machines will be the sales locations added. Howard pointed out that Coke is sold at various price points everywhere from vending machines at Motel 6 to the cocktail lounges at the Four Seasons Hotels. Third, Starbucks is seeking to become a big player in instant coffee and grocery outlets through the VIA instant coffee. Why not have better tasting coffee at home and gain a larger share of the cups consumed each day? Starbucks intends to execute this vision while paying stockholders 35% to 40% of the

after-tax profits in the form of dividends. Overall, you couldn't leave the meeting without being excited about the future of Starbucks.

While we met with Starbucks, I asked Howard Schultz and Troy Alstead if they realized how similar their vision and strategy looked to the one being executed at Nordstrom. Nordstrom is selling premium products with maximum service at their flagship stores. They are enticing fashion conscious discount shoppers to their Nordstrom Rack stores. These bargain hunters get great brands and aren't coddled quite as much as at the premium level. Lastly, Nordstrom meets your shopping needs at home through its Nordstroms.com online store. Once again, three fronts to their vision as well. Nordstrom raised its dividend 25% last week. It was recently on the front of the New York Times Business section and the author was raving about their first Nordstrom Rack store in Manhattan. Both of these premier brand name companies look attractive, especially after the recent pullback in the US stock market.

Abbott Labs was one of the companies featured in Jim Collins book, "Good to Great". They announced last week that they are paying \$3.7 billion to buy the largest maker of medicine in India. We have argued that the demand for medicine (vaccines, treatments and cures) in both the developing and developed nations would grow as prosperity reached emerging markets and aging populations added demand in countries like the United States. Abbott Labs is one of many strong pharmaceutical companies which have been completely neglected in the stock market the last two years. All this growth comes with regular stock buybacks and consistently good dividend growth. Medicine makers are the smallest percentage of the S&P 500 Index they have been since 1984. We at SCM have a vision of that changing over the next two to three years and have added to our medicine companies including Abbott Labs.

While most stock market participants worry about the short-term direction of stocks, we will keep our eye on "the vision thing".

Best Wishes,

***William Smead***

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