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The Enduring Nature of *Saving Mr. Banks*

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Dear Fellow Investors:

Warren Buffett has admitted that selling Disney in 1966 was the biggest mistake of his entire career.

As long-duration common stock owners, we believe that investors would benefit from seeing the movie, *Saving Mr. Banks*, as a reminder of the wealth-creating potential of investing in wonderful companies over long time-horizons. The firm details the story of Walt Disney's effort in 1961 to convince P.L. Travers, the author of *Mary Poppins*, to allow him to make a movie based on her book.

Disney is a favorite company for us at Smead Capital Management to talk about. First, we've owned it for many years in our portfolio. Second, it's already a long-duration business and is likely to last another 100 years. We like to tell people that their grandchildren's grandchildren are likely to be Disney customers. Third, it is heavy on intangible book value and light on plant and equipment. They brilliantly resell images which were drawn years before. Lastly, the original vision that Walt Disney had of providing wholesome family entertainment is as valid today as it was in 1928 when Walt first etched Mickey Mouse.

If you don't think long-duration investing pays off, consider that Walt Disney began courting Travers for the rights to *Mary Poppins* in 1941 at his daughters urging. By 1961, when Travers finally yielded, Walt Disney Co. (DIS) was a publicly-traded company with a heady reputation as a growth stock.

The movie was a huge blockbuster in1964, but Disney didn't have a large magnitude movie coming out the following year. Without a follow-up blockbuster, Disney's earnings growth slowed in 1965—a major no-no for a glamour growth stock. Buffett recognized that Disney had 200 movies in their library and had a $17 million renovation of the Disneyland theme park ongoing; he swooped in to purchase 5% of the company for $4 million. One of the expenses in the renovation was building what Buffett called, "The Pirate Ride." Buffett was quoted as saying, "I paid five times ride to buy the business." In effect, Disney built "The Pirate Ride" with the money he made from *Mary Poppins*.

You've probably already realized why this is Buffett's biggest mistake. In 1966, he sold his stake in Disney for $6 million and took a $2 million gain. In 1996, when he spoke to students of the University of North Carolina business school, it was worth a billion dollars. Today a 5% stake in Disney is worth over $3 billion. Buffett left over $2.94 billion on the table.

Tracking Disney's brilliant reinvestment of profit is a quintessential example of why we want to be long-duration common stock owners of wonderful companies. The profits from the Mickey Mouse, *Snow White* and other movies went into building Disneyland. Profits from movies and Disneyland went into making *Mary Poppins*. *Mary Poppins*' profits went into "The Pirate Ride" and the park renovation. In the

1990's and 2000's, Disney made a successful movie series out of the "The Pirate Ride" and called it, *Pirates of the Caribbean.*

As a stock picking organization, we are very conscious of the fact that already successful investments need ongoing analysis. The art of stock picking includes the re-investment of unrealized gains. It must be done regularly to create the most wealth over the decades. You run the risk of temporary underperformance to maximize long-duration wealth creation. Disney is a stock which exemplifies this discipline and certainly has corrected itself many times over the decades despite all the smart moves that people like Mr. Disney and current CEO Robert Iger have made.

Moving forward to recent years, Disney has reinvested profits from the *Pirates of the Caribbean* series into the Marvel, *Indiana Jones* and the *Star Wars* franchises. These folks at Disney are terrific at identifying endurable brands in entertainment. **In other words, Walt Disney's effort to convince Ms. Travers to let him make the movie is still blessing shareholders 70 years later**! Only multi-decade owners of Disney have received the benefit of this massive wealth creation. It took him twenty years just to get her to let him make the film, yet we shareholders today are still gaining financial rewards from Walt Disney's persistence.

Ironically, Mr. Buffett didn't mention that he committed the Disney sin of omission twice. He sold for $6 million in 1966 and Disney proceeded to become one of the "Nifty Fifty" growth stocks of late 1972. It sold for 80 times after-tax profits. When the bubble of the "Nifty Fifty" died in the 1973-74 bear market, Disney common stock dropped from $2.43 per share in October of 1972 to $.44 per share in October of 1974. This would have been about three times what Buffett had sold for, but would have put him in position to make his mistake a small sin of omission rather than a massive one.

In conclusion, Disney was a $.07 per share stock at the beginning of 1962 and today trades at over $75. It's P/E ratio of 18 based on 2014 First Call estimates is a premium to the average business in the stock market. Their business of producing "wholesome family entertainment" has endured and is thriving today. The long-duration nature of the business is exemplified by Walt Disney's experience with Ms. Travers and the making of *Mary Poppins.* The lesson for us is to mimic Walt Disney's behavior and his long-duration vision in our ownership of common stocks. Warren Buffett is on record as saying that selling Disney in 1966 was the biggest mistake of his illustrious career, and he reminds us to not make the same mistake.

William Smead

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