A SHARE CLASS - **SVFAX**
I1 SHARE CLASS - **SVFFX**
INVESTOR SHARE CLASS - **SMVLX**

SMEAD
value fund

877.701.2883 | SMEADCAP.COM

1ST QUARTER 2019 (3/31/19)

Performance

Average Annualized Total Returns as of March 31, 2019

	ONE MONTH	QTR	YTD	ONE YEAR	THREE YEAR	FIVE YEAR	TEN YEAR	ANNUALIZED SINCE INCEPTION 1/2/2008
SVFFX	-0.22%	8.18%	8.18%	7.54%	11.48%	8.65%	16.66%	8.34%
SVFAX (w/ load)	-5.98%	1.90%	1.90%	1.13%	9.06%	7.10%	15.57%	7.40%
SVFAX (w/o load)	-0.25%	8.11%	8.11%	7.30%	11.24%	8.37%	16.25%	7.97%
SMVLX	-0.25%	8.13%	8.13%	7.25%	11.17%	8.36%	16.38%	8.11%
RUSSELL 1000 VALUE	0.64%	11.93%	11.93%	5.67%	10.45%	7.72%	14.52%	6.54%
S&P 500 TR INDEX	1.94%	13.65%	13.65%	9.50%	13.51%	10.91%	15.92%	8.32%

Investor Shares Gross Expense Ratio 1.31% A Shares Gross Expense Ratio 1.27% I1 Shares Gross Expense Ratio 1.02%

Performance data quoted represents past performance; past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance of the fund may be lower or higher than the performance quoted. Performance data current to the most recent month end may be obtained by calling 877-807-4122. Performance for SVFAX (w/load) reflects maximum sales charge of 5.75%. Performance for SVFAX does not reflect maximum sales charge of 5.75%. If reflected, the load would reduce the performance amount quoted. SVFAX imposes a 1.00% redemption fee on purchases of $1,000,000 or more that are redeemed within 18 months of purchases. Performance data does not reflect the redemption fee. If it had, returns would be reduced.

Investor Class shares of the Fund commenced operations on January 2, 2008. I1 Class shares of the Fund commenced operations on December 18, 2009. Performance shown for I1 Class shares prior to its inception reflects the performance of Investor Class shares. Class A shares of the Fund commenced operations on January 24, 2014. Performance shown for Class A shares prior to its inception reflects the performance of Investor Class shares, adjusted to reflect Class A expenses.

Dear Shareholder

"Envy is a lousy sin, because it is no fun!"
—Charlie Munger, Berkshire Hathaway Annual Meeting

The Smead Value Fund (SMVLX) had a way above average return in the first quarter of 8.13%, but the indexes had way, way above average returns of 13.65% for the S&P 500 Index and 11.93% for the Russell 1000 Value Index. Growth stomped value, oil ripped higher and the more risk people took, the more they got rewarded. Therefore, low-quality value beat high-quality value. To top it off, investors guaranteed 3% in long-term quality bonds also made a ton of money.

We had lots of big winners in the first quarter, led by Target (TGT), American Express (AXP) and Lennar (LEN). Recession fears caused the Federal Reserve Board ("the Fed") to back off on interest rate increases (a.k.a. lower interest rates for longer). This motivated stock buyers to bet on millennial spenders and home buyers.

Our losers were retailers like Walgreens (WBA), grocery stores like Kroger (KR), and a biotech like Amgen (AMGN), which got discounted on the heels of weaker guidance. In case you have no access to information, the hare has beaten the tortoise, with few interruptions, for three to four years. All three of these are "Steady-Eddie" stocks in a market that desires appreciation disconnected from past morals and skills (see below).

We've trained ourselves to resist envying common stock ownership formats which rely on momentum or expensive stocks getting more expensive. Our portfolio ended the quarter five percent cheaper relative to the index than it started the year, and to buy it this cheap, you'd have to go back to the year 2012. We'd love to make around eight percent every quarter, but a stock market which historically makes six percent capital gains plus dividends annually is not likely to give that out very often.

Stock Market Morality

History of Stock Market Morals

Virtually every major athletic and business endeavor has been governed over long periods of time by a set of standards or morals. In basketball it helps to be tall, in baseball it helps to run fast and throw hard and in football it helps to be physically strong. In business it helps to have capital, sales, profits and free cash flow. We believe that the morality of common stock investing gets unhinged after an extended period of easy money and low interest rates.

The history of the stock market lays some reliable markers for long duration investors when it comes to these morals. First, in the long run, a basket of the cheapest of the stocks in the S&P 500 Index has outperformed the expensive ones by 3.6% per year on average over the last 90 years (Source: Ibbotson Associates). Therefore, the moral of the story is that when you have the chance, we believe you should look to bargain prices in relation to earnings if you seek to outperform indexes and other stock picking organizations.

Second, research from Fidelity Investments driven by the legendary investor, Peter Lynch, showed that long term equity performance was attached to earnings growth. He argued that when the noise of stock price movements was backed out after ten years, that price performance followed closely with earnings growth.

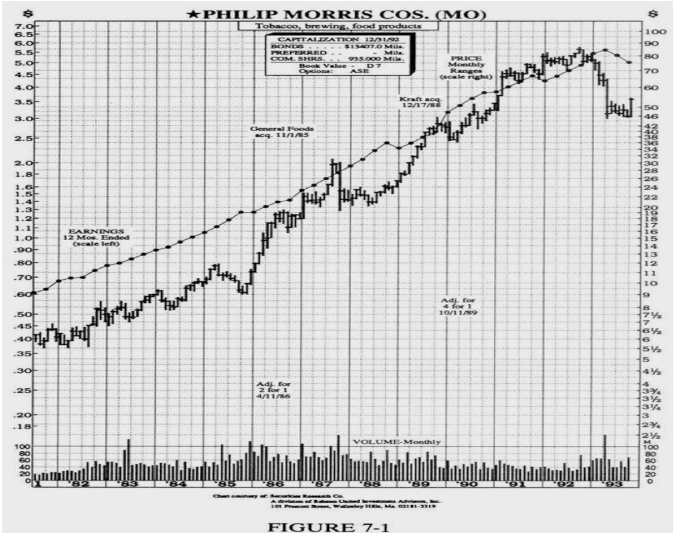
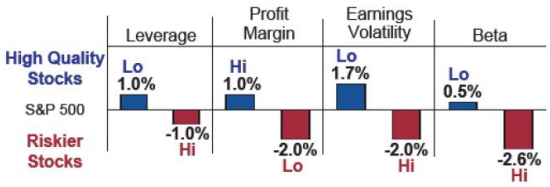


FIGURE 7-1

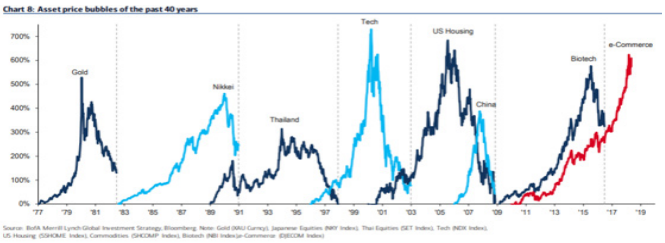
Source: Securities Research Co. and Philip Morris. Data for the time period 7/1/1981 – 12/31/1993.

Next, Ben Inker from Grantham, Mayo, Van Otterloo, proved via a 24-year study that companies with stronger balance sheets, companies which maintain high levels of profitability and companies with very consistent earnings produce index-exceeding performance. There is a morality to these factors in common stock selection.



Source: GMO, monthly data for the time period 1/1982-12/2003.

Fourth, history shows that parabolic manias can make people temporarily rich on paper but end up crushing the capital of anyone who isn't lucky enough to get out before the financial euphoria episode collapses.



Source: DoubleLine Funds, BofA Merrill Lynch Global Investment Strategy, Bloomberg. Data for the time period 1/1/1977 – 12/31/2018.

In his book, *A Short History of Financial Euphoria*, John Kenneth Galbraith describes the morals of what to do if you are in such a set of pioneering investments:

> *"We quickly forget financial disasters and the circumstances that brought them about, and as a consequence, when the same or closely similar circumstances arise again, sometimes in just a few years, they are hailed by a new, often youthful, and always extremely self-confident generation as a brilliantly innovative discovery in the financial and larger economic world." For Galbraith, it becomes a consistent cycle of "illusion to disillusion and back to illusion…. There can be few fields of human endeavor in which history counts for so little as in the world of finance."*

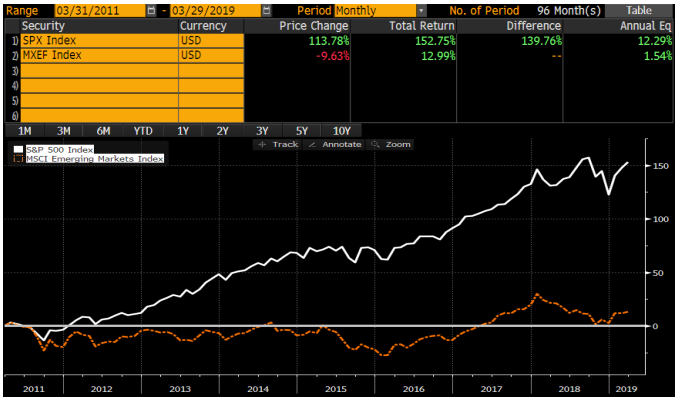
Why have morals underperformed the last five years?

Unfortunately for investors like us who are conscious of these historical truths, the last five years have pulled investors as far away from the long-term fundamental standards as we've seen other than in 1999 and 2000. Why has the market given up on proven historical morals?

It begins with the fascination of pioneering use of technology in artificial intelligence (AI) and data analytics. This technology has overtaken investor attitudes just like other euphoric episodes. In the process, this has pretty much divorced stock pricing away from historical morals and standards. Faith in what is viewed as a nearly-riskless secular trend now rivals the faith in the "Nifty Fifty" stocks of 1972, the dot-com stocks of 1999 and those wonderful new 500 million middle class citizens of emerging markets from 2011.

Source: Bloomberg. Data for the time period 6/30/1972 – 6/30/1975.

Source: Bloomberg. Data for the time period 12/31/199 – 3/28/2003.



Source: Bloomberg. Data for the time period 3/31/2011 – 3/29/2019.

The wonderful demographics and the easy money/low rates of the last nine years haven't yet coalesced into a secular trend that active investors can ride. When we look at housing starts adjusted by population and think about combining 95 million millennials with trillions of dollars of financial-crisis-induced liquidity, we wonder if you need artificial intelligence or any significant level of intelligence to appreciate how much demand for housing we can have.

Figure: Industries where Millennial will transform sectors as their spending dwarfs that of the Boomers
2018-2028

Category	Millennials	Boomers	Total	Millennial share of Growth
Mortgage interest and charges	163.4%	(32.4%)	43.9%	93%
Kids Apparel	110.9%	(27.3%)	47.3%	87%
Other apparel products and services	155.4%	(18.3%)	46.2%	86%
Footwear	148.2%	(18.6%)	46.2%	85%
Apparel and services	130.7%	(16.5%)	46.5%	77%
Vehicle finance charges	106.3%	(28.5%)	44.9%	68%
Other entertainment supplies, equipment, and services	124.6%	(34.7%)	42.8%	67%
Furniture	116.4%	(16.9%)	46.2%	67%
Toys, hobbies, and playground equipment	98.6%	(4.7%)	48.3%	66%
Cellular phone service	105.2%	(18.9%)	46.1%	63%
Gasoline and motor oil	107.6%	(9.0%)	47.5%	59%
Household furnishings and equipment	126.9%	(3.9%)	48.2%	59%
Tobacco products and smoking supplies	102.1%	(21.1%)	45.3%	58%
Vehicle purchases (net outlay)	95.4%	(12.6%)	46.9%	56%
Vehicle rental, leases, licenses, and other charges	102.5%	(12.0%)	46.9%	55%
Maintenance and repairs	115.5%	(7.8%)	47.3%	55%
Pets	125.4%	(9.8%)	47.3%	54%
Alcoholic beverages	98.6%	(8.0%)	47.6%	52%
Vehicle insurance	118.7%	(11.7%)	47.0%	51%
Small appliances, miscellaneous housewares	101.3%	(12.7%)	47.1%	50%

Source: Fundstrat

To be *transformed* by Millennials…

These industries will see a big substitution of consumer spending—Millennials replace Boomers

Source: Fundstrat, "The Long Game," 2019 Strategy.

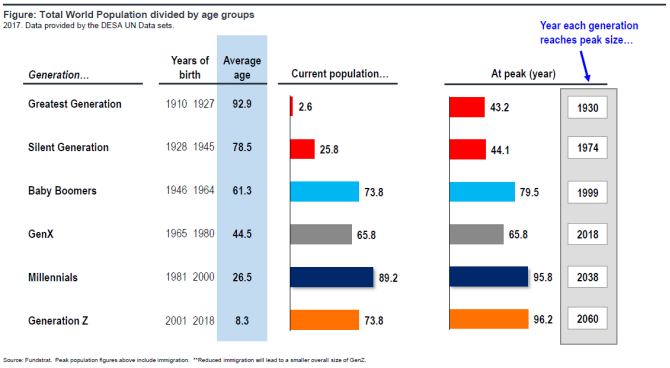
Since the Fed can't see the whites of the millennial boom eyes, they have panicked into a lower-for-longer mode on interest rates, which turns right around and unhinges stock market participants further from the morals and standards which have governed success in long-term time periods. When money is cheap and economic growth is hard to come by, the stock market loves a good revenue growth stock story or investing in the hottest new technology company.

The good news is we have entered the crazy stage. Wall Street stands ready to flood the stock market with initial public offerings (IPOs) of money-losing companies whose business model is built around the AI and data analytics, which matches up with the current financial euphoria episode. First Lyft and Uber, along with a panoply of other money-losing tech unicorns will make their debut. My 39 years on Wall Street helps tell us that exciting companies priced without a connection to the morals and standards of history are not only sexy as hell, but have a high probability to take your investment results to Hades in the next ten years.

How to trust the morals

First, we believe, from the accompanying chart, that you can trust the demographics to lead you to the secular trends which can make you money without selling your investment discipline's soul to the financial euphoria devil.

Figure: Total World Population divided by age groups
2017. Data provided by the DESA UN Data sets.



Source: Fundstrat. Peak population figures above include immigration. **Reduced immigration will lead to a smaller overall size of GenZ.

Source: Fundstrat, "The Long Game," 2019 Strategy.

Second, we will stick to our eight criteria for common stock selection which have never changed or wavered. These criteria are anchored in the standards and morals which have proven true over all recorded stock market history. When the demographics and easy money explode together, having your own capital, generating high free cash flow and showing consistent profitability could shine as interest rates rise. When tech goes through one of its many cyclical downturns, we will smile as we watch investors around us wail and gnash their teeth.

Lastly, the CEO of one of our largest holdings, Discovery Inc. (DISCA), said recently that the most popular channel among 25-year-old U.S. women is HGTV. Outside of HGTV, the most popular show among those same 25-year-old women is TLC's 90-Day Fiancé. Unless we are missing something, this is not very different from what polls said 20 or 40 years ago. The difference today is these 25-year-old women are the most college educated group in U.S. history and will be in charge of future households and businesses. Their interests are tied much closer to the historical standards and morals which have driven long-term equity performance. Thank you for being on the journey of patience with us.

William Smead
Portfolio Manager

Tony Scherrer, CFA
Co-Portfolio Manager

Cole Smead, CFA
Co-Portfolio Manager

The recent growth in the stock market has helped to produce short-term returns for some asset classes that are not typical and may not continue in the future. The price-earnings ratio (P/E Ratio) measures a company's current share price relative to its per-share earnings. Alpha is a measure of performance on a risk-adjusted basis. Beta is a measure of the volatility of a security or a portfolio in comparison to the market. Growth investing is focused on the growth of an investor's capital. Leverage is using borrowed money to increase the potential return of an investment. Momentum is the rate of acceleration of a security's price or volume. Parabolic mania, or a bubble, is an economic cycle characterized by the rapid escalation of asset prices followed by a contraction. Profit margin is calculated by dividing net profits by net sales. Quality is assessed based on soft (e.g. management credibility) and hard criteria (e.g. balance sheet stability). Value is an investment tactic where stocks are selected which appear to trade for less than their intrinsic values. Volatility is a statistical measure of the dispersion of returns for a given security or market index.

The information contained herein represents the opinion of Smead Capital Management and is not intended to be a forecast of future events, a guarantee of future results, nor investment advice.

The Smead Value Fund's investment objectives, risks, charges and expenses must be considered carefully before investing. The statutory and summary prospectuses contain this and other important information about the investment company, and it may be obtained by calling 877-807-4122, or visiting www.smeadfunds.com. Read it carefully before investing.

Mutual fund investing involves risk. Principal loss is possible.

The following were the top ten holdings in the Fund as of 3/31/2019: NVR Inc. 6.31%, Amgen Inc. 6.19%, Discovery Inc. Class A 6.16%, American Express Co. 5.99%, Target Corp. 5.43%, Aflac Inc. 5.09%, Berkshire Hathaway Inc. B 4.87%, Walgreens Boots Alliance Inc. 4.69%, JPMorgan Chase & Co. 4.23%, and Bank of America Corp. 4.20%. Fund holdings are subject to change at any time and should not be considered recommendations to buy or sell any security. Current and future portfolio holdings are subject to risk.

The S&P 500 Index is a market-value weighted index consisting of 500 stocks chosen for market size, liquidity, and industry group representation. The Russell 1000 Value Index is an index of approximately 1,000 of the largest companies in the US equity markets; the Russell 1000 is a subset of the Russell 3000 Index. The Russell 1000 Value Index measures the performance of the large-cap value segment of the US equity universe. It includes those Russell 1000 companies with lower price-to-book ratios and lower expected growth values. The Russell 1000 Growth Index measures the performance of the large-cap growth segment of the U.S. equity universe. Information is provided for information purposes only and should not be considered tax advice. Please consult your tax advisor for further assistance.

Small- and Medium-capitalization companies tend to have limited liquidity and greater price volatility than large-capitalization companies.

Active investing generally has higher management fees because of the manager's increased level of involvement while passive investing generally has lower management and operating fees. Investing in both actively and passively managed funds involves risk, and principal loss is possible. Both actively and passively managed funds generally have daily liquidity. There are no guarantees regarding the performance of actively and passively managed funds. Actively managed mutual funds may have higher portfolio turnover than passively managed funds. Excessive turnover can limit returns and can incur capital gains.

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