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Billy Joel and the Art of Investing

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Dear Fellow Investors,

We believe that Billy Joel is perhaps the most preeminent singer/songwriter of the U.S. baby-boom generation. Art, like Billy Joel's music, has a tendency to mirror culture and economics. Thanks to his recent tour in the U.S., we were reminded of how four of Billy's greatest hits speak to our current circumstances in the stock market and give incredible advice about how to behave as investors over the next ten years.

1. "Allentown" 1982

In 1982, the U.S. was wrenching from a deep recession with unemployment hitting a high of 10.8%. Manufacturing jobs were being lost to cheaper labor in other countries as big labor priced itself out of world market competitiveness. They asked for wage increases to match inflation and forgot that folks in foreign countries could do the work cheaper. Billy wrote and sang:

*"Well we're living here in Allentown
And they're closing all the factories down
Out in Bethlehem they're killing time
Filling out forms
Standing in line"*

The investing crowd thought a reduction in emphasis on manufacturing in the U.S. would permanently hurt GDP growth. History shows that household formation led by baby boomers, and the houses and cars which they bought, overwhelmed the economy from 1982 all the way to the late 1990's. This is a good picture today as the media and major political figures argue that a shrinking middle class, off-shoring of manufacturing jobs and economic inequality mean a bleak future for GDP growth in America. It is our opinion that the 86 million Americans between 21 and 39 years of age are preparing to overwhelm the economy over the next ten years in a similar way.

2. "We Didn't Start the Fire" 1989

*"We didn't start the fire
It was always burning
Since the world's been turning
We didn't start the fire
No we didn't light it
But we tried to fight it"*

For my 36th consecutive year in the investment business, investors are using societal, political and cultural problems as a reason to not invest in quality common stocks. Billy did a great job of reminding everyone that external problems “were always burning, since the world was turning.” On a recent business trip to Europe, U.S. presidential politics was what folks wanted to talk with us about. There has never been a good time for investors to get distracted by Marilyn Monroe, Richard Nixon and military conflicts like the Bay of Pigs and be pulled away from strong companies at attractive prices.

3. “Pressure” 1982

*“But you will come to a place
Where the only thing you feel
Are loaded guns in your face
And you'll have to deal with
Pressure”*

Even though he hasn't been very successful in his own investments, Billy Joel explains the feelings of those who do participate in the common stock market. Investment returns are really earned when the markets are going against you, not when they are going your way. Many managers who run a high-conviction and low-turnover stock picking discipline will run into situations “Where the only thing you feel are loaded guns in your face.” One of the all-time great investors, Howard Marks, put it this way:

“I'd say the necessary condition for the existence of bargains is that perception has to be considerably worse than reality. That means the best opportunities are usually found among the things most others won't do. After all, if everyone feels good about something and is glad to join in, it won't be bargain-priced.”

When investors are making money in sectors and industries you are not participating in, you feel incredible pressure to conform to the crowd. Jeremy Grantham describes successful investing as opening yourself up to career risk. Grantham argues that you must be willing to stand against the crowd in a way that makes investors feel incredibly uncomfortable and run the risk of losing some of your investors along the way.

4. “Vienna” 1977

Billy Joel reminds investors to have patience:

*“Slow down you're doing fine
You can't be everything you want to be before your time
Although it's so romantic on the borderline tonight (tonight)”*

He argues for reduced portfolio management activity:

*“Slow down you crazy child
Take the phone off the hook and disappear for a while
It's alright, you can afford to lose a day or two (oooh)
When will you realize...Vienna waits for you?”*

He reminds investors that long-duration investing is a marathon:

*“But you know that when the truth is told
That you can get what you want
Or you can just get old
You're gonna kick off before you even get halfway through (Oooh)
When will you realize...Vienna waits for you?”*

We believe Billy Joel’s art offers very good advice for long-duration common stock investors. First, the economy of the U.S. will include its share of creative destruction and carry a short-run human toll as it makes its changes over the years. Second, those who let major political, economic and social upheavals chase them away from owning good quality common stocks have damaged their returns historically.

Finally, we believe successful execution of portfolio management must include significant time stretches where the pressure to conform to the crowd of investors and to their beliefs will produce extreme discomfort to the high-conviction portfolio manager. Lastly, Vienna, in this case, represents the ultimate goals of long-duration common stock investing. It means meaningful long-term outperformance versus both peers and benchmark indexes. We’d like to think ‘Vienna’ is waiting for us.

Warm Regards,



William Smead

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