



William Smead
Chief Executive Officer
Chief Investment Officer

Buffett Whispers of Danger

Dear fellow investors,

In the 2017 Berkshire Hathaway Annual Letter, Warren Buffett told us what he is doing, and, in as quiet a voice as he could use, what he says to do. Our readers will not be surprised at our summation of Buffett's letter, but here we go anyway.

1. Buffett explains his bet of the S&P 500 Index against a basket of hedge funds:

"The bet illuminated another important investment lesson: Though markets are generally rational, they occasionally do crazy things. Seizing the opportunities then offered does not require great intelligence, a degree in economics or a familiarity with Wall Street jargon such as alpha and beta."

We argue that paying 250-times trailing earnings for Amazon (AMZN) while they seek to ruin everyone's business is not rational and, to us, borders on crazy.

2. Buffett shares an excellent reminder on stock picking discipline:

"A final lesson from our bet: Stick with big, "easy" decisions and eschew activity. During the ten-year bet, the 200-plus hedge-fund managers that were involved almost certainly made tens of thousands of buy and sell decisions. Most of those managers undoubtedly thought hard about their decisions, each of which they believed would prove advantageous. In the process of investing, they studied 10-Ks, interviewed managements, read

trade journals and conferred with Wall Street analysts."

Academic research shows that high conviction and low turnover creates alpha and Buffett reminded us. The astute investor, Michael Price, says it this way, "The more decisions I make, the dumber I am."

3. Buffett is very quietly and subtly warning about overheated security prices:

"In the next 53 years our shares (and others) will experience declines resembling those in the table. No one can tell you when these will happen. The light can at any time go from green to red without pausing at yellow."

When major declines occur, however, they offer extraordinary opportunities to those who are not handicapped by debt. That's the time to heed these lines from Kipling's If:"

*'If you can keep your head when all about you are losing theirs . . .
If you can wait and not be tired by waiting . . .
If you can think – and not make thoughts your aim . . .
If you can trust yourself when all men doubt you . . .
Yours is the Earth and everything that's in it."*

Buyer beware! We will patiently wait for our "if" to come along and are willing to look "foolish" from time to time and stay in our discipline.

4. Buffett appears to agree with our piece last week, Minority Report:

“What investors then need instead is an ability to both disregard mob fears or enthusiasms and to focus on a few simple fundamentals. A willingness to look unimaginative for a sustained period – or even to look foolish – is also essential.”

We look very unimaginative to not own “disrupters” and occasionally look foolish when Amazon hits its latest milestone. At Smead Capital Management, we buy

companies which fit our eight criteria for stock selection when mob fears hit them and shun the great futuristic enthusiasms. Lastly, we tell you about what we are doing and say it loudly, SO YOU CAN HEAR! 🐦

Warm regards,



William Smead

Source: Berkshire Hathaway Inc. 2017 Annual Letter

The information contained in this missive represents Smead Capital Management’s opinions, and should not be construed as personalized or individualized investment advice and are subject to change. Past performance is no guarantee of future results. Bill Smead, CIO and CEO, wrote this article. It should not be assumed that investing in any securities mentioned above will or will not be profitable. Portfolio composition is subject to change at any time and references to specific securities, industries and sectors in this letter are not recommendations to purchase or sell any particular security. Current and future portfolio holdings are subject to risk. In preparing this document, SCM has relied upon and assumed, without independent verification, the accuracy and completeness of all information available from public sources. A list of all recommendations made by Smead Capital Management within the past twelve-month period is available upon request.

This missive and others are available at www.smeadcap.com.

