SMEAD capital management

Missive

AUGUST 6, 2026

Circle Of Competence

Dear fellow investors,

As many of you know, our team at Smead Capital Management has studied the thinking and investment careers of Charlie Munger and Warren Buffett. In today's Go-Go artificial intelligence-dominated stock market, we'd like to walk you through the concept of the Circle of Competence.

Charlie Munger's concept of the circle of competence is a mental model that states you must know the exact boundaries of what you understand and stay within them to avoid costly mistakes. It is not about how large your circle is, but how well you define its edges.

We like to buy meritorious companies that meet our eight criteria for stock selection. Then we hold our winners to a fault, because most of your best gains come via long-term (10-plus year) holding periods. At the beginning of placing these investments, we must have a clear understanding of the business, and typically, we have no special ability in predicting what will happen in the immediate future. Among our group of 25-30 companies, we must understand the history of the industry, the economics of the industry, investor psychology as connected to the industry and the math as it pertains to the price we are paying versus our estimate of the present value of the future income stream.

In the history of our strategy, we have owned common stocks in most of the major S&P 500 sectors. However, none of those investments had anything to do with any special vision of the future. Instead, we felt that pessimism surrounding the company or industry had been overdone, and a patient investor could capitalize on it over five to ten years.

In 1999, eBay (EBAY) went public and the stock went from $18 per share to over $300 per share very quickly. I made fun of the stock and considered the price of the shares ridiculous. However, I thought that the concept was brilliant (The New York Stock Exchange of garage sales).

By November of 2008, eBay was trading for $11 per share. They had $3 in cash, no debt. They owned 100% of PayPal (PYPL), 100% of StubHub and 100% of Skype. Virtually everyone hated the company because it wasn't dominating e-commerce like Amazon (AMZN) was, but it was capital-light in a way that Amazon wasn't.

Our circle of competence includes a lack of envy towards people who attempt to understand how the future will go for hot industries, especially in technology. Munger said it best about envy, "Envy is a really stupid sin because it's the only one you could never possibly have any fun at!" But we are good at simple math. Skype was sold to Microsoft for more than they got for the other 65% of Skype. StubHub was sold to private equity investors and PayPal shares were distributed to shareholders on a one-for-one basis. We sold out of our PayPal stock for an average of $130 per share and still hold half of our original eBay shares at around $113 after selling some on the recent Ryan Cohen Meme trade.

Another good example was in 2020 when everything shut down due to the COVID-19 virus. People were convinced that nobody was going to want to shop anytime soon. Fortunately for us, we were in Arizona at the time and the state only shut down for 60 days ending on May 15th that year. My wife is the consummate shopper as she has numerous grandchildren and comes from an extensive line of good shoppers. When we got to the reopening on May 15, 2020, I told her that we would go to the Tanger Outlet Mall by the Glendale Stadium, where we had attended a Super Bowl.

After she was done being shocked (I rarely shop), we drove across town and parked near the Nike outlet. When the doors opened, 50 people were waiting in line to enter, two at a time, for 15 minutes. We had all the information we needed to make additional investments in Macerich (MAC) around $6 per share and our first purchases of Simon (SPG) around $60, the premier mall operators, and in Simon's case, the number one outlet owner.

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Imagine our frustration watching investors lose any faith in our work because we readily admit that we have no competence in figuring out who will be the surviving success stories in artificial intelligence. In past maniacal markets like the 1873 Railroad Mania, the 1925 Florida land boom, or the Dotcom Bubble in 1999, there were a small number of success stories. The railroad industry was largely unfruitful for the original speculators involved, as was the Florida land grab. As survivors from the 1999 bubble, eBay and Amazon took years to emerge after losing more than 80% of their peak valuations. Will it be any different this time?

As long as we stick to our circle of competence, we believe our investors' futures are going to be bright relative to those who are enjoying ephemeral maniacal market riches.

Play The Long Game,

Bill Smead
Chairman & Chief Investment Officer

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