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'Little Book' sums up stock strategy; 'Magic' formula relies on faith, patience  
Kerry Hannon

Joel Greenblatt's *The Little Book That Beats the Market* is pitched not to the swells of Wall Street but to the novice individual investor.

Greenblatt, the founder of hedge fund firm Gotham Capital, has taken what he has learned about investing and written this skinny, pocket-size book.

His goal: to explain how to make money in terms that even his five kids could understand. "I figured if I could teach them how to make money for themselves, then I would be giving them a great gift."

Greenblatt, a Columbia Business School professor and an investor for 25 years, says, "I believe I can teach you (and each of my children) to be one of them" -- meaning, a successful investor.

*The Little Book That Beats the Market* is simple and sincere; Andrew Tobias, author of *The Only Investment Guide You'll Ever Need*, writes the introduction.

The formula works if you have faith and are patient enough to follow his guidance -- over time, Greenblatt says.

Greenblatt's formula is based on Warren Buffett's investment principles: Invest in good companies when they are cheap.

According to Greenblatt, his formula historically has beaten the market for nearly two decades. Although he does not name the stocks, he claims that from 1988 through 2004, the high-return/low-price stocks of 30 of the largest 2,500 companies had returns of 22.9% annually.

Simple enough. But how do you find these stocks? "The truth is you don't need an MBA to beat the market," he writes.

But there's no fairy godmother on Wall Street. "If your stockbroker is like the vast majority, he or she has no idea how to help you! They don't get paid to make you money. The plain fact is you are on your own." That said, you have no business investing in individual stocks on your own, he says.

His magic formula promise: "If you just stick to buying good companies (ones that have a high return on capital) and to buying those companies only at bargain prices (at prices that give you a high earnings yield), you can

achieve investment returns that beat the pants off even the best investment professionals."

He has a free (for now) website, [www.magicformulainvesting.com](http://www.magicformulainvesting.com), which screens companies using his criteria. He advises individual investors to buy a basket of 20 or 30 top stocks over the course of a year and turn them over on a strict schedule, depending on how they perform. He does not mention a minimum amount to invest.

Be forewarned, though. The formula may or may not work over "shorter" periods, which can often mean years, not days or months. Good things come to those who wait and, in this case, Greenblatt means that it takes three, four or even five years to show its stuff. After a year or two of performing worse than the market averages, most people won't stick with it. But you've got to "really believe in it deep down in your bones."

Even if you don't drink the Kool-Aid, you will learn about the technique of value investing from a pro. Greenblatt boils investment jargon down to what you need to know as succinctly and humorously as possible. Along the way -- and it won't take you more than two hours tops -- you're given a tutorial on bonds, stock shares and prices, earnings yields, return on capital and more. The appendix, which is "not required reading," adds a more detailed, strategic commentary.

It might be hard for less-schooled investors to understand why the "magic" formula makes sense and to stay with it when things get bleak, but the hard part is just getting started, he counsels. That's true for investing, period.

The International Herald Tribune  
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The (not so easy) way to beat market indexes;  
MARKETPLACE by Bloomberg  
Chet Currier

In an age that celebrates passive index investing, the hottest new book in financial circles takes the opposite side of the argument.

We're talking about "The Little Book That Beats the Market," by the hedge fund manager Joel Greenblatt, a \$19.95 volume from John Wiley & Sons that has jumped right up there with the likes of "Your Best Life Now" and "The Chronicles of Narnia Boxed Set" on best-seller lists.

No, no, you can't beat the market, the indexers always tell us it's a "random walk," since everything that can be known or surmised about a stock is already built into its price. Greenblatt says he hopes to see "a random walk spoiled."

If his premise is simple, the promises that have been heaped up around it are extravagant. "It provides a 'magic formula' that is easy to use and makes buying good companies at bargain prices automatic," the dust jacket declares.

And what is this secret? In Greenblatt's own words, it is to "find above-average companies that we can buy at below-average prices." Above-average companies are identified by high returns on capital. Below-average prices are identified by high earnings yields, which is another way of saying low price/earnings ratios.

Back to the dust jacket: "You can achieve investment returns that beat the pants off even the best investment professionals and the top academics. In fact, you can learn how it's possible to more than double the annual returns of the stock market averages."

"But there's more," it adds. "You can do it all by yourself. You can do it with low risk."

"Best of all," it concludes, "once convinced that it really works, you can choose to do it for the rest of your life."

Wow! Investing was never this easy. But veterans of the game have seen such claims before and long ago learned to view them with a skeptical eye. Let's not judge a book by its cover. Let's look at what ordinary readers have to say about it. Simple as the book's basic idea may be, the reaction to it has been complicated.

"Excellent!" said the first reader review I perused on the Web site of the bookseller Amazon.com. A second sneered, "This is a fairy tale." The last comment I checked summed it up: "An easy quick read, some good points, some big problems."

One intriguing aspect of Greenblatt's case is the way he deals with the nagging question of how any market-beating system, no matter how good, can keep working once it is popularized. After all, if some investors are going to beat the market, there must be others who get beaten.

"The magic formula appears to work very well over the long term," Greenblatt writes. Even so, he says, its history shows it may produce subpar results for periods of a year or two.

"Most people just won't wait that long," he argues. "Their investment time horizon is too short. Even professional money managers who believe their strategy will work over the long term have a hard time sticking with it."

Hmmm, everyone will not do this because many will find it too hard. So much for the dust-jacket claim that "successful investing can be made easy for investors of any age."

Greenblatt delivers admirably on some other promises: The book can be read in two hours or so. It is good-humored throughout, and it contains one of the clearest, most entertaining explanations you'll ever see of the ideas underlying value investing.

I plan to pass it along to people close to me who struggle to understand investing and the markets. It's that readable.

At the same time, I plan to tell them I regard the whole idea of beating the market as a red herring, which is defined by the American Heritage Dictionary as "something that draws attention away from the central issue."

Beating the market is, at best, a misguided goal for most individual investors. When a child's college tuition comes due, it matters not whether you beat the market or not. The only pertinent question is, do you have the money to pay the bill?

Real-life investment plans should be geared to such real-life goals, with careful attention to risk as well as reward not to an abstraction like beating the market. That is for the professionals.

I also plan to urge my near and dear ones to pay closest attention to the parts in which Greenblatt talks about what makes investing not so easy after all. That would include Chapter 12, in which he states, "When it comes to Wall Street, there ain't no tooth fairy."

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Library Journal Reviews  
January 15, 2006

The Little Book That Beats the Market  
C. Geck

Greenblatt is renowned for his spectacular business prowess; among his many accomplishments are averaging returns of 40 percent or better for more than a decade; starting his own lucrative private investment firm, Gotham Capital; and currently serving as an adjunct professor at Columbia Business School. Here he shares his stock selection wisdom with the novice investor. His writing is never condescending or beyond comprehension. In fact, he takes great joy in explaining ideas in simple terms and using arithmetic that he claims even his young children can understand. He also delights in sharing with readers his "magic formula" of finding quality bargain stocks. Lighthearted, witty, and humorous, the overall presentation is a great start for learning about investing and can be used as an alternative to comparable titles in the Dummies series. Recommended for public libraries as well as undergraduate collections for a non-textbook understanding of investing principles; readers who like Greenblatt's style may then continue with his earlier and more advanced work, *You Can Be a Stock Market Genius*.

-C. Geck, Kean Univ., Union, N.J.