

Contents

Preface	xi
Acknowledgments	xiii
PART ONE	
The Foundation of Quantitative Value	1
CHAPTER 1	
The Paradox of Dumb Money	3
Value Strategies Beat the Market	9
How Quantitative Investing Protects against Behavioral Errors	23
The Power of Quantitative Value Investing	30
Notes	32
CHAPTER 2	
A Blueprint to a Better Quantitative Value Strategy	35
Greenblatt's Magic Formula	36
It's All Academic: Improving Quality and Price	45
Strategy Implementation: Investors Behaving Badly	54
Notes	59
PART TWO	
Margin of Safety—How to Avoid a Permanent Loss of Capital	61
CHAPTER 3	
Hornswoggled! Eliminating Earnings Manipulators and Outright Frauds	63
Accruals and the Art of Earnings Manipulation	64
Predicting PROBMs	72
Notes	79

CHAPTER 4

Measuring the Risk of Financial Distress: How to Avoid the Sick Men of the Stock Market	81
A Brief History of Bankruptcy Prediction	83
Improving Bankruptcy Prediction	85
How We Calculate the Risk of Financial Distress	86
Scrubbing the Universe	89
Notes	91

PART THREE

Quality—How to Find a Wonderful Business	93
---	-----------

CHAPTER 5

Franchises—The Archetype of High Quality	95
The Chairman's Secret Recipe	96
How to Find a Franchise	99
Notes	112

CHAPTER 6

Financial Strength: Foundations Built on Rock	113
The Piotroski Fundamentals Score (F_SCORE)	114
Our Financial Strength Score (FS_SCORE)	119
Comparing the Performance of Piotroski's F_SCORE and Our FS_SCORE	122
Case Study: Lubrizol Corporation	123
Notes	126

PART FOUR

The Secret to Finding Bargain Prices	127
---	------------

CHAPTER 7

Price Ratios: A Horse Race	129
The Horses in the Race	130
Rules of the Race	133
The Race Call	134
A Price Ratio for All Seasons	141
The Official Winner	142
Notes	143

CHAPTER 8

Alternative Price Measures—Normalized Earning Power and Composite Ratios	145
Normalized Earning Power	147
Compound Price Ratios: Is the Whole Greater than the Sum of Its Parts?	150
Notes	163

PART FIVE

Corroborative Signals	165
------------------------------	------------

CHAPTER 9

Blue Horseshoe Loves Anacott Steel: Follow the Signals from the Smart Money	167
Stock Buybacks, Issuance, and Announcements	169
Insider Traders Beat the Market	173
Activism and Cloning	176
Short Money Is Smart Money	179
Notes	182

PART SIX

Building and Testing the Model	185
---------------------------------------	------------

CHAPTER 10

Bangladeshi Butter Production Predicts the S&P 500 Close	187
Sustainable Alpha: A Framework for Assessing Past Results	189
What's the Big Idea?	191
Rigorously Test the Big Idea	196
The Parameters of the Universe	206
Notes	208

CHAPTER 11

Problems with the Magic Formula	211
Glamour Is Always a Bad Bet	216
Improving the Structure of a Quantitative Value Strategy	218
Our Final Quantitative Value Checklist	222
Notes	228

CHAPTER 12**Quantitative Value Beats the Market 229**

Risk and Return 231

Robustness 239

A Peek Inside the Black Box 249

Man versus Machine 257

Beating the Market with Quantitative Value 262

Notes 264

Appendix: Analysis Legend 265**About the Authors 267****About the Companion Website 269****Index 271**