

Marshall, Kenneth Jeffrey – Good Stocks Cheap

McGraw Hill, 2017, [Equity Investing] Grade ★★★★★

Value investing might be described as the practice of buying and holding stocks that according to the investor's best judgment have a suitable probability of having a substantially higher value than current price. The insistence on such a margin of safety is in part a philosophical issue but – similar to the requirement of tilting probabilities in one's favor – is also a very practical issue of applying a suitable and rational investment process. In *Good Stocks Cheap* Kenneth Jeffrey Marshall, an investor and academic who teaches value investing and asset management at the Stockholm School of Economics and at University of California, shares his personal value investing process.

Although the author covers the basics of value investing it has to be said from the outset that this is not a book for anyone seeking deeper knowledge of finer nuances on the topic. This is a book on process. And mainly the process of selecting stocks to invest in. As such, important topics worthy of entire books in themselves, such as capital allocation, insider dealings, selling positions, moats etc. are covered in one or a few pages each. The benefit of this book instead lies in how explicit it is in penciling out how to actually perform the craft of value investing. Execution matters greatly in the potential success of investing.

The title is an apt description of the content as value investing in this case refers to the currently popular quality-compounding genre, not investing in low valuation multiple, bombed out, deep value stocks. This is a Joel Greenblatt Magic Formula-type of stock selection but with a quality bent.

The author suggests a sequential process of analytical steps for a stock to pass to qualify as a portfolio holding. Firstly, by looking to a number of angles the investor must be able to say that he truly understands the business of the company. If not, he should move on to another candidate. Secondly, it must qualify as a good business. In this Marshall looks to the historical financial success of the company, the indications of whether this

success will continue into the future and of how shareholder friendly the management is. After weeding out bad businesses the next needle(s) to pass is the parallel decision on if this good stock is also cheap judging from the absolute level of a number of valuation multiples and if the investor in the process of analyzing the qualities and inexpensiveness of the stock has been free from biases. If all boxes are ticked it could be warranted to allocate 10% of the portfolio to the stock. It's quite easy to visualize what a flowchart of the process would look like - and Marshall offers his version. He subsequently presents a short chapter on idea generation that logistically perhaps should have been placed earlier in the book. Further, there is no advice on what to do during the times when no stocks qualify, as all good stocks are expensive. Is cash then the preferred option?

The text is written in an accessible language making it suitable for the novice investor, but is not at all dumbed down due to this. Writers who have taught value investing – such as Ben Graham and Bruce Greenwald – have often had the chance to refine how they explain topics to an audience and this gives great clarity to their texts - so also in this case. The one section that doesn't come out as well is chapters 6 to 10 that gives a combination of a basic accounting course and further shows which adjustments to the accounting Marshall thinks necessary to render the financial ratios best suited for his process. This section would have benefited from incorporating a case study to be followed throughout the chapters. Instead the reader in appendices and 10-K's online get to work with the accounting of GAP, but few readers ever read appendices or look up online annual reports in parallel to reading a book. Still, this section is already a quarter of the book – perhaps Marshall didn't want to burden the text further?

Growth and momentum has ruled this investment cycle. Value investing isn't chic anymore. Thus, now might be the time to catch the turning tide. This book shows one way forward.

Mats Larsson, May 6, 2018